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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 592

WILLIAM H. OSBORN, CHANNING F. MacNEIL, LEWIS C. ADAIR, ET AL., *Appellants*

vs.

THOS. W. OZLIN, WILLIAM MEADE FLETCHER AND LESTER HOOKER, ETC., ET AL., *Appellees*

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF VIRGINIA

BRIEF FOR THE APPELLEES

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APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF VIRGINIA

BRIEF FOR THE APPELLEES

PRELIMINARY STATEMENT

While this suit technically is prosecuted by thirty-four surety and casualty companies and the branch managers of three of them against the Virginia authorities charged with the duties relating to the enforcement of the insurance laws of the State, the real question presented involves the jurisdiction of Virginia to exercise her police powers to regulate rates and other matters in connection with Virginia coverage insurance contracts negotiated and made outside of Virginia, principally in New York City.

It is believed that the facts established by the evidence and the application thereto of the appropriate principles of law can be more clearly and satisfactorily discussed by dividing this brief into two sections or parts, the first part to be directed principally to a development of the facts and legal principles relied on to establish the State's jurisdiction and the reasonableness of the statutory regulations, and the second part to be in the nature of a reply to the brief filed by the appellants. The appellees will accordingly adopt this plan.

PART I.

FACTS AND LEGAL PRINCIPLES RELIED ON BY APPELLEES

OPINION BELOW

The opinion of the court below, pursuant to which the decree appealed from was entered, is reported in 29 Fed. Supp. 71.

GROUNDS OF JURISDICTION

The appellants challenge the validity of certain Virginia statutes as in violation of due process of law, and, in addition thereto, the branch manager appellants claim they are deprived of the equal protection of the laws because discriminated against in favor of salaried agents of mutual insurance companies. The appeal is pursuant to sections ~~228~~ 238 and 266 of the Judicial Code.

STATEMENT OF THE CASE

Section 4221-a of the Virginia Code divides the producing agents and employees of stock fire, surety and casualty insurance companies into two main classes, first, those who work on a regular salary, and, second, those who are compensated exclusively by commissions. The former is designated as either a "State Agent," "Special

Agent," or a "company representative." The same form of license is issued to each of them. The appellant branch managers come within this class. The commission agent is designated a "Resident Agent" and is so licensed. The classification is based upon the well established customs, usages, and practices of such stock insurance companies, their agents and employees. A full statement of the respective duties and functions of these agents and salaried representatives is contained in paragraph 17 of appellees' answer (R. 34-37). The chief distinction between the functions of the "Resident Agent," generally known in the business as a "producer," and the salaried representatives of the companies is that the commission or resident agent contacts the public and the policy-holders are regarded as his customers or clients (Op. R. 43), not those of the company, while the salaried representatives secure new resident agents, instruct and encourage them in their work, collect premiums due from resident agents, and generally represent the company in dealing with resident agents. Briefly stated, the business of the salaried representative is to contact the resident or producing agent, that of the agent to contact the prospective insured in producing business, and the assured in servicing the contract after same has been procured (Op. R. 46-7). "Whenever a branch manager negotiates a policy directly with an assured, the rule of the National Association of Insurance Agents, in which most insurers have acquiesced, requires that the contract be closed through one of the manager's commission agents who is paid the full producer's commission. The Manager's function is to develop his territory through ordinary producing agents and to supervise and assist them in the production of desirable business" (*Id.*).

In conformity with this custom, the Virginia statutes provide that all contracts of these types of insurance shall be made through the commission or resident agent, and that he shall countersign the contract and be paid full commissions. As to business produced in Virginia, the requirement of the statute conforms to existing customs (Op. R. 54), and this is true also as to fire insurance contracts produced outside the State, except that it has been customary for the resident agent to receive only half of the commissions where the contract was negotiated by a producer outside the State (Op. R. 61-2). In recognition of this custom in the fire insurance business, the Virginia statute permits the nonresident licensed broker who negotiates the contract to be paid half of the commission in casualty and surety contracts. (See appendix for quotation of the pertinent statutory provisions.)

The effect of the statutory provisions complained of is to require the casualty and surety companies to conform to the usages and customs of the fire insurance business; that is, to require that a Virginia resident commission agent be associated with a nonresident Virginia licensed broker in all Virginia coverage casualty and surety contracts produced by such a broker outside of the State. The fire insurance companies also come within the provisions of the statutes, but, since no substantial change is made in their customary business methods, they have made no complaint. But the casualty and surety companies, as to business produced outside the State, have never insisted on a Virginia resident agent being associated with the servicing of such contracts, and the brokers in New York, where most of such business originates, have stubbornly resisted any such practice.

Customs and Practices with Respect to Virginia Contracts Produced in New York

As stated in the opinion of the court below:

> "Brokers are rarely found except in large cities. In New York they produce virtually all the contracts, for the demand for insurance is so concentrated and has assumed such tremendous proportions that insurance is bought rather than sold. The producer represents the buyer, and remains free of company affiliation in order to use the assured's concentrated bargaining power to its best advantage when dealing with the various companies" (R. 46).

Three New York City brokers testified as witnesses for the appellant insurance companies. They seem to regard the insurance business as being patterned after the New York Stock Exchange. Thus the witness Thomas, 75% of whose business covers in other states, says the broker "knows his markets pretty well, or he should know them," and that his "business is pretty well spread all over the *Street* among the larger companies" (R. 791). Otis said, "We know our markets pretty well" (R. 859), while Gessner, the third broker, testified that the assureds have one or two brokers "sound out the market" to ascertain the best and most attractive "price" obtainable (R. 923). "The party assured by a policy produced outside of Virginia is occasionally a natural person who keeps his records and manages his business outside the state, and has interests in Virginia and elsewhere. But ordinarily, the assured is a large national corporation, incorporated in any of the states, with its central office in New York, Chicago or some other great business center. One company plaintiff in-

sures a mercantile corporation against the risk of public liability arising from the operation of 258 stores scattered throughout Virginia. Nation wide manufacturers, distributors, financial institutes, contractors, dairy companies, public utilities and others purchase contracts outside of Virginia to cover exposures which they have in that state. These contracts are produced almost exclusively by brokers operating in large cities where the national corporations have their principal offices, and the great majority of this business is produced in New York City, which has become the center for the insurance business in this country. Many of these out-of-state producers are licensed by Virginia as non-resident brokers" (Op. R. 48-9).

The term "market" is a very appropriate one to apply to the purchase and sale of Virginia insurance in New York, because the insurance companies bid for contracts at the lowest price. Many of the large casualty and surety companies are affiliated with fire and other types of insurance companies, and these groups may bid a price on the entire coverage of of the national corporations, including fire, surety, casualty, inland marine and all other lines except life insurance (R. 804). A contract of this kind combines into one "price" all of the assured's risks in all the states in which the assured does business (R. 125-7). Contracts of this type the court below refers to as "hotchpotch" or "multi-coverage" contracts. There are from ten to twenty brokerage firms in New York who place over a million dollars of premium business a year with one insurance company (F. & C.), and in some instances greatly in excess of that amount (R. 120). Some of the states of coverage regulate the premium rates for all or a part of the lines sought to be covered in those states while others do not.

Thus the insurance company may nominally appear to charge the rate fixed in Virginia for coverages here while completely nullifying the fixed premium rates for a particular line by adjusting the net price with component items in which the premium rate is not regulated and fixing these items at ridiculously low amounts (R. 916-918). A large national corporation usually permits several brokers to invite bids from the insurers on the same risk or combined risks, with the result that the tion operates to reduce the insurer's bid "price" (R. 805, 880). This competitive bidding for insurance often becomes so keen that the broker will consent to a reduction in his customary commissions, and this reduction operates to reduce the insurer's bid "price" (R. 805, 880-1). The insurer seeks to justify this by the argument that the acquisition cost factor in the premium rate is being reduced. The obvious effect of the practice, however, is a rebate by the broker to the assured of a part of his commissions, a practice which is forbidden by the statutes of Virginia and many states.

For many years the states have sought, by legislation, to regulate insurance rates and to prevent rebating and other discriminatory practices in the insurance business, and such legislation has been invariably encouraged and sustained by the decisions of this Court. In fact the propriety, fairness, wisdom and salutary effect of such regulatory legislation has rarely, if ever, been questioned in recent years. Yet the clear and obvious effect of the practices followed by insurance brokers has been to completely wipe out and nullify these regulatory statutes. By scrambling several hundred risks, each of which should be the subject of a separate contract, into one hotchpotch the insurer brings forth a "price" which he bids against another insurer (R. 805, 880, 917-8, Op. R. 52-3).

The necessary result of this practice is to completely eliminate Virginia's insurance rate regulations. The broker Thomas testified, "We don't deal so much in rates as what the ultimate net cost is going to be" (R. 805). The insurers use the term "equity rating" with respect to lines where no rate is fixed by law. In a hotchpotch contract the amount charged for a risk of this kind is purely arbitrary and when the term "equity rating" is used it really means there is no rate and the company fixes the cost to suit itself (R. 917-918). The broker Gessner testified with respect to hotchpotch contracts that "in practically all cases they are subject to either experience or equity rating, some form of special rating other than manual rates."

It cannot be denied that this reduced price for these hotchpotch contracts operates as a discrimination against other policy holders in Virginia and in the other states, and is clearly in violation of the spirit of the Virginia statutory prohibition against rebates. It also has the effect of discriminating against the local Virginia agent who may not rebate any part of his commission, as well as against Virginia and other fire insurance companies who do not have casualty and surety company affiliates. Any chance the Virginia agent might otherwise have of negotiating a contract with such an assured for local Virginia coverage, is completely eliminated by this practice, as also is any chance of such a fire company to secure the fire insurance business alone, or a casualty company to secure the casualty business alone.

An effort is made by appellants' witness Nicholls and by appellant Adair to justify the existence of these brokers by reason of alleged extraordinary services the "Broker's" *engineering* organizations are able to render.

Their testimony, fairly interpreted, however, shows that these so-called services are merely gestures and that the insurance companies themselves maintain like organizations in Virginia and in the various states of coverage, which are more advantageously situated to render engineering service, and which actually do render all such engineering service as can be really helpful in connection with such contracts. (Nicholls R. 147, Adair R. 240-1, Murphy R. 713.) In fact the witness Nichols inadvertently let the cat out of the bag when he said (R. 118):

> "The successful broker today gives such services that will *make the assured believe that he is actually earning his commission.*"

This witness knew of only one case where any broker had rendered any so-called "service" in Virginia (R. 148). The Richmond Branch Manager Adair never heard of a case where the assured derived any benefit from this so-called "service" of a nonresident broker (R. 243-4).

It very clearly appears from three of plaintiffs' witnesses, who are New York brokers, (Thomas, Otis, Gessner) that they perform little, if any, of certain types of service which an agent on the scene of the risk usually renders. Only one of these brokers had any engineering service and this consisted of one man for the entire United States (R. 801). Their evidence clearly shows that their services are, as a matter of fact, restricted to those which can be rendered in New York, and do not extend to those types of service, which in the nature of things, a local impartial agent alone can render. The broker Gessner testified that a very small percentage of

brokers have an engineer and that is mostly in the fire insurance line (R. 927).

It is quite clear that the so-called broker is, in reality, a barnacle on the business; a parasite, boring in where he is not needed and rooting out the legitimate agent. By pitting the companies against one another in competition for his favors he has demoralized rate standards and eliminated the local Virginia agent from participation in the cream of what should properly be classified as Virginia business (R. 921). Not only that, but he has almost completely eliminated the producing agent in New York City. The laws of New York prohibit him from brokering *life* insurance contracts.

The detrimental effect of this practice upon the outside states where these national corporations carry on a local business is at once obvious. Their citizens conducting an insurance agency business are utterly helpless to compete with these foreign brokers and the benefit of this very lucrative business is lost to Virginia and the other outside states. Virginia is thus deprived of taxing what would be legitimate incomes of her citizens which they are entitled to earn, and of sources of livelihood for them which would promote prosperity within her borders and alleviate her burdens of providing relief to the unemployed. It is obvious also that the reduced insurance costs and rebates granted the national corporations, such as chain stores, give them an unfair advantage over the local merchant and other businesses with which the national corporations compete in Virginia.

Furthermore, the State of coverage expends funds to provide fire protection to minimize losses under fire insurance policies; provides safe highways and traffic officers

in reducing liabilities from motor vehicle liability policies; inspects and regulates the operation of machinery in plants where employees are covered by workmen's compensation insurance; and provides police protection and courts in preventing defalcations under surety bonds. As an aid in carrying this burden the State is by this statute requiring the association of a local resident agent in connection with all such insurance contracts and is invoking the active help and cooperation of such local agent to render the assistance customarily given by them in domestic business to prevent the happening of the events resulting in the losses insured against (R. 381-2).

Then, again, this legislation establishes a policy that every *assured* shall have the benefit of the services of a local resident agent, impartial as between the insurer and the assured, in all cases of Virginia coverage. Such an agent should carefully examine the policy or contract before issuance to determine whether it fairly and justly conforms to the needs of the assured, and is required to countersign the policy or contract as evidence that he has performed this service for the assured (R. 358, 367, 374-6). He should keep an eye upon the subject of the insurance and the progress of events relating thereto during the time it is in force, advising both the assured and the insurer from time to time as to any matters needing attention. (See testimony of appellants' witnesses DeJarnette, R. 269-274; Boswell, R. 302; Clark, R. 330-336; Tabb, R. 356-361, 366-9. See also appellees' Exhibit "A", R. 279-280.) Obviously the Virginia agent will not, and cannot be expected to, render this service unless he is adequately compensated. The only means of accomplishing this purpose as to such contracts and policies issued at the request of these New York and

other out of state brokers is to require the association with such a broker *on a compensatory basis* of an impartial resident Virginia agent in connection with both the issuing and servicing of every such contract or policy.

In 1921 Virginia legislation, as stated in the opinion below, "was interpreted by the State Insurance Commissioner to require that all insurance on persons or property within Virginia should be issued under a policy separate from insurance on persons or property in any other state; that if the Virginia risk should be covered under a general cover contract form, it should include only Virginia property; that the rates should be those applicable to risks covered as published by the Rating Bureau of which the insurer was a member; and that the policy should be issued through and signed by a resident agent who should receive the usual commission, but this last provision did not apply to company employees who received a fixed salary."

"Prior to the Act of 1938, the resident agent who countersigned a policy produced outside the state performed no useful function in the production, underwriting or servicing of the contract. The appellants' brief states: 'Companies have never observed the mandate of the statute not to make contracts (outside of Virginia) except through licensed Virginia agents. * * * When, because of the compulsion of the law of a state of coverage, the company must secure the countersignature of a licensed agent there, he may countersign only a "law rider" or a "countersigning endorsement." He may sign one of a number of "underlying contracts" retained by the company, while a "master contract" is delivered to the assured.' Customarily, contracts produced outside of Virginia have been countersigned by the general

agents and branch office managers without compensation. They have not performed any of the services habitually offered the assured by a resident producer; but these services have been rendered by the nonresident producer and by the companies' salaried employees, such as engineers and adjusters, particularly the latter, when the matter has been one that could not be handled by a producer remote from the locality of the coverage. Prior to the Act of 1936, the Virginia resident agent statute requirements have had no real effect on the production of the contracts" (Op. R. 53-4).

The purposes, therefore, which the challenged statutes are designed to accomplish may be briefly stated as follows:

FIRST: To adjust the above mentioned competitive inequalities between the Virginia resident agents and the New York and other large city brokers and agents with respect to commissions on Virginia coverage insurance contracts and policies now being negotiated by such nonresidents (Op. R. 51).

SECOND: To adjust the similar competitive inequalities between Virginia insurance companies none of which have group affiliates, and those which are members of such groups, now existing in favor of the latter, enabling them to combine in one hotchpotch contract the several types of risks insured against by all companies in the group (Op. R. 51).

THIRD: To adjust similar competitive inequalities between Virginia merchants and other businesses and chain stores and other national corporations (Op. R. 51).

FOURTH: To secure the services of Virginia resident agents (a) for the benefit of all holders of contracts and policies issued by such companies in the exercise of their Virginia privileges and franchises, and (b) for the benefit of the State as an aid in providing efficient and economical fire, motor patrol, police protection and other functions of government incidental to the matters covered by such contracts and policies (Op. R. 60-61).

FIFTH: To assist in bringing within the regulatory control of the State as to rates, taxes and other matters insurance contracts negotiated or made outside the State (Op. R. 52-3, 61).

The *means* by which the statute undertakes to accomplish these purposes are the requirements (a) that every such contract and policy shall be countersigned by an impartial commissioned Virginia agent, and (b) that such agent shall be compensated to the extent of at least one-half the producer's commission customarily paid to him where he alone negotiates a similar contract and thereafter services same.

The reasonableness of these statutory provisions, as well as the State's jurisdiction to enact same, depend, of course, upon their application to the well established customs and practices of the surety and casualty insurance companies and their agents and employees, which will now be referred to.

ESTABLISHED CUSTOMS AND PRACTICES OF THE SURETY AND CASUALTY INSURANCE BUSINESS

This business may be divided into three main divisions: (a) the securing of contracts or policies of insurance, from the premium for which the company derives its principal income; this is usually called the production

division; (b) the performance on the part of the company of the obligations imposed on it by such contract or policy, embracing what are usually spoken of as the engineering and claims divisions; and (c) the investment of its capital, surplus, and reserves. With this investment feature we are not here concerned, so it may be eliminated from further consideration.

The Production Division includes the fixing of premium rates in so far as they are not controlled by law; underwriting, or passing on the desirability of risks; and the soliciting and negotiating of contracts of insurance.

The premium rate for any particular line of coverage is primarily based on the average loss experience in that line. As to any particular assured with any substantial volume of coverage in certain lines this average loss experience is adjusted to his individual experience history or record, and his premium rate is raised or lowered to conform thereto. Each premium rate contains as a component part thereof a factor called "acquisition costs" which embraces the commission or compensation paid, or to be paid, to the agent who negotiates and procures the insurance contract and renders the requisite service with respect to same throughout its duration (Op. R. 47).

All contracts of the appellant companies are written through commission agents, and they are compensated out of that part of the premium dedicated to that purpose as above pointed out. These agents furnish, operate and maintain their own offices at their own expense, and generally are agents for a number of insurance companies. The assureds with whom they negotiate insurance contracts are universally regarded as customers or clients of the agent and not of the insurance company. The agent therefore occupies a dual relationship. For some purposes he is the agent of the insurer while, at the

same time, he is agent of the assured for other purposes. To each he occupied a fiduciary relationship, and to properly perform *his* obligations to *each* he must act fairly and impartially to the end that the insurer and assured shall each fairly and impartially perform their duties and obligations to one another. In case of disagreement over loss adjustments or any other dispute he acts as an impartial mediator to see that justice is done to both (Op. R. 45-6).

The service of the agent to the assured begins with the negotiations. He studies the problems presented in the particular situation confronting the assured, considers what type of contract will best serve the desired end and what changes in conditions may be made to reduce the cost of the desired protection. Having determined these matters he next sees that the contract itself is in proper form, contains appropriate provisions to meet the assured's needs, and that same is properly classified for premium rates. Thereupon he countersigns the contract and delivers it to the assured.

But this by no means completes the service the agent is to render. He studies the loss experience of his client, the assured, and makes suggestions for changes in methods of operation so as to reduce losses, such as accidents under workmen's compensation or automobile liability insurance policies, or other suggestions appropriate to the particular line of coverage carried by the assured.

He sees to it that the engineering and inspection services which the insurer is either under obligation or is willing to provide from its service departments in the State are furnished and utilized to the best advantage, and that the assured receives the benefit of any

changes in the contract or policy provisions to which he becomes entitled from time to time as a result of such service, or as a result of amendments and modifications of applicable rules, regulations or laws. He appears before regulatory and rate making bodies to the end that his clients' risks shall be properly classified and other appropriate action taken with respect thereto. He prepares proofs of claim and, as before mentioned, acts as an impartial mediator between the assured and the company in cases of loss adjustments or other disputes. He is always available to the assured for consultation and advice with respect to the interpretation of the contract, the assured's duties thereunder or any other matters relating to the coverage.

This commission agent, who in Virginia negotiates the insurance, and thereafter performs the various duties above described, from the standpoint of the insurance company is a producer of premiums and the company applies to him the term "Producer." The Virginia statutes designate him a "Resident Agent," and require that all contracts, wherever made, which have the situs of the risk in Virginia, and which insure against loss from risk or events which, if they occur at all, will occur in Virginia (except traveling risks) shall be made "through" this commission "Resident Agent." This word "through" is interpreted by the Virginia law enforcing authorities (the appellees), as meaning that whenever such a Virginia coverage contract is made in New York, or any other place, the company shall associate a Virginia "Resident Agent" with the nonresident broker or agent who negotiates the contract with the assured. The statute further provides that this Virginia "Resident Agent" "through" whom, as an associate,

the contract is made, shall receive at least fifty per cent of the commission which he could have received if he alone had negotiated and thereafter would service the same contract. The statute also requires that this "Resident Agent" shall countersign each such contract, regardless of where negotiated or made. "The important object of the statute is to require that all policies shall be placed by a resident agent, who shall take a real and not merely a nominal share in the placing of the business and in the performance of the contract. Of this main purpose the requirement of countersignature by the resident agent is only a minor and incidental part of little importance except as indicating that the resident agent shall become an active factor in the business, especially when coupled with the major requirement that he shall be entitled to the whole commission of which he must retain one-half. The latter requirement, it is reasonable to conclude, will probably lead to greater participation on the part of the resident agent and he will be expected to render to the company and to the assured all the services of which he is capable. The tendency will be to create a more efficient agency force with the result that the local interests of the insured will be better served" (Op. R. 60-61).

Of course, the gravamen of the complaint in this suit is the requirement of the statute that a Virginia "Resident Agent" must be associated, on a compensatory basis, with the New York or other nonresident broker or agent who may negotiate the contract outside of this state.

The natural persons appellant in this suit, Osborne, McNeil and Adair, designate themselves as "Agents plaintiff" in the complaint. The application of the term

"Agents" to these three appellants is somewhat confusing. As a matter of fact, while it is true that from a legal standpoint these three appellants are "legal agents" of their companies, just as the president and every other officer of such company is a "legal agent," it is no more in conformity with insurance practices to refer to said persons appellant as "Insurance Agents" than it would be to refer to the President of the Company as an "Insurance Agent." The truth of the matter is that these persons appellant are "Branch Managers" or heads of branch offices set up, established and operated solely at the companies' expense, by the companies by whom they are employed. These officers are, to all intents and purposes, miniature *home offices*, and the "Branch Managers" are employed on a salary basis to operate and manage them. They never have received any commissions, and have never been permitted by their companies to receive any. Whenever in past years, as appears to have occasionally happened, they have negotiated an insurance contract directly with an assured, and they have invariably closed the contract through one of their "Resident Agents" and paid him the full commission he would have received had he himself negotiated it (Op. R. 47). But it is not the duty or function of these branch managers to negotiate with the assured. Their duties are to assist and supervise existing "Resident Agents" and to establish new "Resident Agencies." Generally speaking, the only negotiating the "Branch Manager" does directly with the assured is when he is requested by the "Resident Agent" to assist him in securing the business. The "Branch Manager" deals with the "Resident Agent," the "Resident Agent" deals with the assured. The "Branch Man-

ager" represents the company in dealing with the "Resi
dent Agent," while the latter, as above set out, is the im
partial representative both of the assured and of th
company, and sees that the assured's interests are fairl
protected.

While the insurance contracts (which the state'
power to regulate is here challenged) are made outsid
the state, they invariably contemplate the exercise of th
insurance company's Virginia license privilege in thei
performance. Most of these contracts are made upo
the understanding, express or implied, that they will b
continually serviced by the insurer's engineers and in
spectors in Virginia. All of them contemplate that in cas
of loss, the company's Virginia claim adjusters will ren
der service in settling claims (Op. R. 49, 51, 60).

Frequently the company's license privilege is exercise
even before the contract is made, as in cases where th
company requires its Virginia inspectors to examine an
report upon conditions pertaining to the risk befor
making its decision to accept or reject the same (R
601). This exercise of the franchise from the State t
transact an insurance business in Virginia, whether suc
exercise be actual or potential in specific instances, con
fers upon the State the jurisdiction to regulate the entir
transaction from its inception as will appear from th
decisions of this Court hereinafter referred to.

The legislation here challenged has the effect o
bringing to some extent within the control of Virginia
a business transaction which is but incidental to th
operation of a local branch industrial plant or store o
other local unit of a large national corporation. Th
local unit of the parent operation is, in reality, local bus

ness. It is universally recognized that one of the chief causes of our present economic and industrial dislocation has been the centralization of control of the nation's business in New York. The witness Nicholls, one of the appellants' New York branch managers, testified that this tendency of centralized control is increasing in the insurance business (R. 123-4, 149-150), while the appellant Adair, the Richmond insurance branch manager of the same insurance company, testified that nearly all of the large industrial plants being established in the Valley of Virginia are controlled in New York (R. 233). The practices prevailing there in the insurance business, as disclosed by the testimony in this case, present a typical illustration of how that city's centralized control acts as a huge vacuum, sucking in tribute and toll from the state where the real industrial activities take place. At page 351 of the record appears a public statement made January 7, 1939, by Hon. William O. Douglas, now an associate justice of this Court. The associated press account of the statement is as follows:

> "Chairman William O. Douglas of the Securities and Exchange Commission yesterday said, in an interview, the South would have a large regional stock exchange of its own if S. E. C. succeeds in decentralizing the nation's financial structure.
>
> "He said a main objective of S. E. C. was to take financial control from New York and Chicago in order that control of local business may be brought home 'where it belongs'."

This is but one of many statements emanating from economists, business leaders and lawyers of the highest standing deploring the harmful and destructive effect of

the centralization of business in New York. Statutes of the type here challenged are designed to remedy this evil, and may be very instrumental in accomplishing this beneficial purpose. While this statute regulates only one of the many problems relating to out of state contracts, it does present a test case of the jurisdiction and power of the several states to regulate the rest of them. If the state is without power to enact the regulation here challenged, then it is powerless to prevent the destruction of its rate regulating powers by forbidding hotchpotch contracts covering Virginia risks, or to remedy rebating by agents or brokers and the consequent unfair competition between such agents and brokers, or to remedy any of the other evils which may now exist or may grow up with respect to these insurance contracts.

ARGUMENT

The complaint in this case raises certain constitutional questions with respect to the following statutory provisions:

A. The requirement of section 4222 of the Virginia Code that casualty, surety and fire insurance companies, licensed to do business in the State, shall make all contracts of insurance or surety *covering risks in Virginia* "through regularly constituted and registered resident agents" regardless of whether the insurance is completely negotiated outside the State solely through nonresident agents or brokers.

B. The provision that such a contract so negotiated shall be countersigned by such a Virginia resident agent and that he shall receive and retain one-half of the pro-

ducer's commission customarily paid to him when he himself negotiates a similar contract.

Before discussing the disputed questions of constitutional law involved, it will be helpful to refresh the memory of the Court by calling attention to a few undisputed underlying basic principles, which have been well established, but which necessarily relate to and are interwoven and connected with the controverted questions to be considered. These may be stated as follows:

(1) *Contracts of insurance are not commerce at all, and when made between citizens of different states are not interstate commerce and are not affected by the commerce clause of the Federal Constitution.*

Paul v. *Virginia*, 8 Wall. 168, 19 L. ed. 357;
New York Life Ins. Co. v. *Deer Lodge County*, 231 U. S. 495, 58 L. ed. 332, and the many cases therein reviewed;
National Ins. Co. v. *Wanberg*, 260 U. S. 71, 67 L. ed. 136;
Bothwell v. *Buckbee*, 275 U. S. 274, 72 L. ed. 277.

(2) *The insurance business is clothed with a public interest and, in all of its phases, is subject to the regulatory police power of the State.*

German Alliance Insurance Company v. *Lewis*, 233 U. S. 389, 58 L. ed. 1011;
Hooper v. *California*, 155 U. S. 648, 39 L. ed. 297;
National Ins. Co. v. *Wanberg, supra.*

In this case Mr. Chief Justice Taft said:

"The decision of this court in *German Alliance Ins. Co.* v. *Lewis*, 233 U. S. 389, * * *, settled the right of a state legislature to regulate the conduct by corporations, domestic and foreign, of insurance as a business affected with a public interest. This includes provision for 'unearned premium fund or reserve; then came the limitation of dividends, the publishing of accounts, valued policies, standards of policies, prescribing investment, requiring deposits in money or bonds, confining the business to corporations, * * * limitation of risks, and other regulations, equally restrictive.' 233 U. S. 412. It includes, moreover, the retrictions of defense to recovery on policies, and the forbidding of stipulations to evade such restrictions" (260 U. S. 71, 73, 74, 67 L. ed. 136, 138).

(3) *As an incident to the exercise of the police power to regulate the insurance business, the State may likewise regulate the business of insurance agents, their powers, duties, functions, compensation, and relations to the insurance companies.*

La Tourette v. *McMaster*, 248 U. S. 465, 63 L. ed. 362, involved the validity of a state statute restricting the granting of an insurance broker's license to residents of the state who had been licensed insurance agents of the state at least two years. In sustaining the statute, the court reiterated the doctrine that the insurance business "is subject to the regulating powers of the state" and said that "it necessarily follows that, as insurance is affected with a public interest, those engaged in it, or who bring about its consummation are affected with the same interest and subject to regulation as it is. A broker is so engaged—is an instrument of such consummation."

In the case of *O'Gorman and Young* v. *Hartford Fire Ins. Co.*, (1930) 282 U. S. 251, 75 L. ed. 324, a New

Jersey statute limited the amount of commissions the insurance companies were permitted to pay fire insurance agents to a "reasonable amount" and required the rates of such commissions to be uniform as to all agents. The statute was challenged as arbitrary and unreasonable, but the court said the statute "deals with a subject clearly within the scope of the police power" and sustained its validity.

(4) *Virginia is without jurisdiction to prohibit an insurance company licensed therein from paying to persons in other states compensation for their services rendered outside of Virginia in negotiating insurance contracts, even though the risk covered relates to persons or property resident in or located in Virginia.*

Fidelity and Deposit Company v. *Tafoya*, 270 U. S. 426.

Virginia's Official Interpretation of the Statutes Involved

It is clear that the Virginia statutes here challenged do not undertake to prohibit or in any manner regulate the compensation or commissions the insurance company may pay to nonresident agents or brokers for services rendered outside of Virginia in negotiating a Virginia coverage contract and that appellants' contention to the contrary is without merit (Appellees' Answer, par. 16-g, R. 33, Moore R. 523-4). Repeatedly in their brief they make the statement that the statute forbids them to make Virginia coverage contracts in other states. But the only act incidental to the making which the statute requires is the countersigning by a resident Virginia agent. This act does not constitute the "making" of

the contract, although it does satisfy the statutory requirement that it be made "through" such agent. The statute is so construed by the appellees, who are the insurance law enforcement officers of Virginia. "Contracts are made 'through regularly constituted and registered agents or agencies of such companies' as required in Code section 4222 when such contracts are countersigned by a 'Resident Agent' as required by said section, even though he does not negotiate the contracts or deliver same or collect the premiums" (Appellees' Answer, par. 16-a, R. 32; Moore R. 524). A contract of insurance is usually considered "made" when the policy is *delivered*. The appellants occupy the position of seeking to enjoin the appellees from punishing them for making these contracts outside the State, although the appellees state on the record that they not only do not intend to do any such thing, but that they construe the statute as permitting the contracts to be so made. Appellees' construction of the statutes is fully set out in par. 16 of the answer (R. 32-3), and proven by the testimony of the Chief Examiner of the Bureau of Insurance (R. 525-8).

Constitutional Questions Involved

The appellants challenge the validity of the Virginia statutes upon two grounds: (1) That the legislation is an attempt by the state to extend its regulatory jurisdiction beyond her borders, and over matters beyond her jurisdiction to regulate; and (2) That even if the challenged regulations are within the jurisdiction of the state, same are arbitrary and capricious, and therefore deny due process to all appellants, and also equal protection to the branch manager appellants.

In reply to these contentions the appellees will undertake to maintain the following propositions:

Summary of Argument

I. The statutory provisions here challenged, (as applied to Virginia coverage contracts negotiated outside of the State), do not constitute an attempt by Virginia to extend her regulatory jurisdiction beyond her borders. The regulations are restricted to acts of the insurance company and its agents performed or to be performed within the State, pursuant to and as a consequence of the negotiation of the contract outside of the State.

II. The fact that a Virginia coverage insurance contract is negotiated and made outside the State does not impair Virginia's jurisdiction to regulate the insurance company's acts and transactions performed or to be performed within the State in connection with or pursuant to such contract.

A. All casualty and surety policies and contracts covering Virginia risks require or contemplate acts of performance in Virginia.

B. The making outside of Virginia of an insurance contract which contemplaes, requires, or permits the doing by the insurance company of acts in Virginia, constitutes, as a matter of law, an exercise of the insurance company's license right, or privilege, of doing an insurance business in Virginia.

C. The making outside of Virginia of a contract of insurance involving an exercise of a foreign insurance company's license right or privilege of doing business in Virginia, brings the contract within the jurisdiction and regulatory police power of Virginia.

III. Virginia may prohibit the doing in Virginia by an insurance company licensee of any act in connection with or in the performance of a Virginia coverage contract made by it outside the State in violation of Virginia laws, by the imposition of a fine or by revocation of said company's license to do business in the State.

IV. The fact that a Virginia coverage contract, made by an insurance company licensee in violation of Virginia laws is made outside the State does not impair the jurisdiction of Virginia to revoke the company's license to do business in the State because of making such contract in violation of her laws.

V. The objects and purposes sought to be attained by the challenged legislation are legitimate and proper, and the means employed to that end are not arbitrary or capricious but are reasonable and appropriately adapted thereto.

VI. The branch manager appellants have no standing in court to complain of the statutory regulation requiring insurance companies to make insurance contracts through regularly constituted Virginia resident agents, have them countersign the policies and pay them the usual producer's commission.

VII. The statutory classification of agents and employees of stock insurance companies in Virginia is not arbitrary or capricious, but is a reasonable one.

VIII. This case is not controlled by *Hartford Steam Boiler Inspection and Insurance Company* v. *Harrison.*

A. Whether the statute is unduly discriminatory and therefore denies equal protection is a factual question.

B. Factual conditions in Virginia and Georgia are not necessarily the same.

C. The facts proved justify exempting mutual companies from the Virginia statute.

D. The test of reasonableness, from the standpoint of denial of equal protection, is whether the statute is appropriately adapted to the existing practices of mutual and stock companies, respectively.

E. The appellants are not harmed because the statute does not require mutual companies to compensate their agents on a commission basis.

F. The bill of complaint does not raise the question of equal protection.

These points will be discussed in the order above set out.

I.

The Statutory Provisions Here Challenged, (as Applied to Virginia Coverage Contracts Negotiated Outside of the State), Do Not Constitute an Attempt by Virginia to Extend Her Regulatory Jurisdiction Beyond Her Border. The Regulations Are Restricted to Acts of the Insurance Company and Its Agents to be Performed Within the State, Pursuant to and as a Consequence of the Negotiation of the Contract Outside of the State.

This statute does not forbid the insurance company from negotiating Virginia coverage contracts outside of Virginia, nor does it forbid the company from employing agents or brokers to negotiate same, or from compensating them for their services whether they be licensed by Virginia as nonresident brokers or not. Its provisions, though negatively expressed, are positive in effect. The statute requires the company to make the insurance contract for a Virginia risk through a Virginia resident agent and associate him with the transaction. It requires that this agent shall countersign the policy and also, for his various services, be compensated to the extent of at least half of the customary so-called "producer's commission." The obvious purpose of this is to require certain things to be done in Virginia by the agent residing here in connection with insurance negotiated outside the State. As viewed by the Virginia enforcing authorities, as expressed in a resolution of the Virginia Association of Insurance Agents (Appellees' Exhibit A, hereinafter quoted), and as considered by the individual resident agents, the effect of the statute is to impose on the countersigning agent certain well defined duties (Op. R. 55-6). He should examine the proposed insurance contract to determine whether it is in proper form and whether the premium is correct. He

should also contact the assured, or his or its representative, if practicable, and examine the risk to ascertain whether the coverage or protection provided, as expressed in the contract or policy, conforms to the needs of the assured and whether there are matters of fact pertaining to the risk about which the assured or insurer should be advised before the contract is finally made. It is also considered the duty of the countersigning agent so compensated to render to the company and to the assured throughout the life of the contract the same varied and valuable services which he would customarily render were he alone the agent who negotiated the insurance (Op. R. 55). The testimony of some of *appellants' own witnesses* is convincing that the effect of the statute is to cause the Virginia agents to do certain things and render certain services in this State, both to the insurer and the assured, in connection with these contracts which are very useful and beneficial and in accord with a sound public policy. Prior to the passage of this statute the custom was for a countersigning agent, who was not associated with the contract on a compensatory basis, to countersign same as a matter of course, without even examining the contract, treating the act as a perfunctory one (R. 209, 238-9, 252-3). Of course, neither the assured nor the insurer derived any benefit from such a countersignature and the purpose of the statute in requiring it was completely nullified by the manner in which the act was done. But appellant Adair admitted that resident commission agents *may render* valuable services to nonresident assureds, and that assureds frequently request the association of a Virginia agent with a risk contracted for outside the State (R. 227-8, 280). He further testified that a resident agent

customarily renders valuable services to the assured throughout the life of the contract in cases where he negotiates same (R. 248-9). Nicholls, New York branch manager of the appellant Fidelity & Casualty Company, admitted that a resident countersigning agent may examine into the risk and render valuable services (R. 142-4, 149, 169). This witness further admitted that the Virginia agent customarily renders "incalculable" services throughout the life of the insurance contract he negotiates (R. 165).

Appellants' witness Izard, a resident commission agent of Roanoke, Virginia, who does a large business with nonresident brokers and is opposed to the statute, testified that, before the present statute was passed, the proportion of the commission he would receive in countersigning cases negotiated outside the state was dependent upon the amount of local service the nonresident broker desired him to render, being usually fifty per cent in fire insurance cases, and something less than thirty-five or forty per cent in casualty and surety lines, "it all depends upon the amount of work that you put into the servicing of the risk at the request of the broker" (R. 632).

Appellants' witness Yancy, a commission agent of Harrisonburg, who does a large business with nonresident brokers, and who is opposed to the statute, also testified to the same effect (R. 678-9). This witness stated that, in his opinion, there is no such difference in the service a resident agent customarily renders in connection with fire insurance contracts and that rendered in connection with casualty and surety contracts as would justify paying the resident agent a greater part of the commission in one line than in the other. He

testified that in some cases more service would be required to be rendered by a local producing agent in casualty insurance than in fire (R. 680).

The foregoing testimony of appellants' witnesses pointed out is by no means exhaustive of similar testimony of hostile witnesses. It is sufficient, however, to render it unnecessary to burden the court at this time with a discussion of the testimony of appellees' witnesses on the question of the nature and value of the services customarily rendered by agents local to the risk. There can be no doubt that the effect of the statute is to cause much work to be done *in Virginia* by these agents.

In view, however, of the effort of the appellants here to belittle the extent and value of the services of the commission agent, it is enlightening, and even refreshing, to read from the public statements of two of the insurance company's executives, or representatives, made under circumstances free from the bias and prejudice incident to this litigation. On May 9, 1938, Mr. Charles C. Hannah, Second Vice President of the Fireman's Fund Insurance Company (an affiliate of one of the appellants here) made an address at Atlantic City before the Insurance Conference Management Association. A press release of this speech contains the following:

> "While an agent is legally a representative of the company only, in fact and operation he acts, as well, as broker for the assured. He has come, through practice and custom, to occupy a dual position wherein he advises and represents company and assured with greater facility, dispatch, efficiency, and satisfaction to both than in a single relationship.
>
> * * * * *

"His relation to policyholders is advisory and his self-imposed duties and requirements can be listed in about this order:—

"1. Analysis of insurance needs and recommendation of covers.

"2. Determination of hazards and their possible effect in the way of loss and/or premium cost.

"3. Recommendation of improvement of risk.

"4. Reduction of insurance costs.

"5. Binding of insurance or extension of coverage by endorsement.

"6. Advice as to ways and means of financing premiums.

"7. Prompt attention to losses including suggestions as to procedure, particularly in advance of arrival of adjusters.

"8. Adjustment of small losses.

"In all of these he has immediately available for his use the facilities, experience and assistance of all the companies he represents, including their engineering, service, and adjusting departments, also the rating and inspection associations with which they are associated or affiliated.

"The agent can be and is of valuable assistance to brokers, with whom he works in close cooperation, in the development of the foregoing services, acting in that capacity on their behalf and, it must be said, in splendid loyalty to their interest and with a high regard for the ethics which call for absolute abstention from solicitation of any risk on which he has written the insurance for a broker.

"In his local community, the local agent voluntarily assumes even larger responsibilities in the interest of public welfare which in turn indirectly ben-

efit his customers and companies and in the exercise of which he renders invaluable service. In this capacity he is looked to for leadership and uses his influence and knowledge in the expansion of municipal protection, improvement of construction, removal of conflagration and catastrophe hazards, accident and loss prevention, more adequate policing, and better local regulations generally. The foregoing incompletely lists his opportunities for a real social service but is sufficient for illustration." (Italics supplied.)

Especially noteworthy is the fact that in the foregoing address the insurance executive emphasizes *the value of cooperative service rendered jointly by the broker and the commission agent.*

The other address referred to above was delivered by Mr. Ray Murphy, Assistant General Manager of the Association of Casualty and Surety Executives, an organization to promote the interests of the Casualty and Surety Companies (R. 823). All of the appellant companies are members of this Association (R. 824). This address was printed in pamphlet form by the Association for public distribution. The quotations therefrom copied in the record (R. 353-4) were contained in an editorial in "The Insurance Index" for January, 1939. Mr. M rphy, in this address, made the following public statement:

"Capital stock company insurance is true American insurance. The capital stock casualty and surety companies believe in the American competitive system of private enterprise and they practice it. They adhere to it, even in the face of unfair competition, because they know it gives positive protection at the lowest possible cost and, insurance being a thoroughly human business, they know that every policy that

is written must be supported by *continued service to the assured*, not merely at the time the sale is being made or when the day arrives for renewal, *but throughout the life of the policy, day in and day out.*

"*The only medium through which this service can be rendered consistently is the agent in the field.* He is less the representative of the company whose policies he places than he is the representative of the individual or company he insures. *The capital stock agent is not a salaried employee who must respond to the direction of any one company or group of companies.* He is a business man, doing business in his own local community. His first consideration must be his clients. *That means greater protection for the public than is possible in the case of the direct-writing mutual which operates through a salaried employee.*

"The services that the capital stock agent renders are many and varied. Insurance is a highly competitive business and the agent must be alert and active to survive. That, too, is in the public interest. *From time to time he must advise his clients about changes in policy forms and rates*, giving them full advantage of increased protection. He must be ready to see that his clients receive *full and swift settlement of claims*, and that all of the protective features of the insurance policy *are brought into prompt play* for the benefit of the assured. *All of these things are in the public interest.*" (Italics supplied.)

While the foregoing statements of representatives of the appellant companies are not evidence in this case, they do furnish an adequate basis for judicial notice. The opinions of this Court cite many similar sources of information as to general practices and customs, for instance, the opinion of Mr. Justice Brandeis (dissenting in part), in the case of *Liggett* v. *Lee*, 288 U. S. 541. The weight

to be attributed to information or knowledge of this kind with respect to customs and practices is very great when derived from statements made by two persons in high authority in the insurance business, one of whom is indirectly a representative of all the appellant companies, and the other of whom is a vice president of an affiliate of one of the said companies.

In the light of what these two outstanding insurance executives have publicly said, it is important to note how closely the reaction of the Virginia Association of Insurance Agents to this Virginia statute conforms to the views expressed by these executives as to what the duties and responsibilities of these Virginia commission agents should be under the compensatory provisions of the statute. Appellees' Exhibit A, on February 17, 1939, was mailed out to all members of the Association (R. 346). It is a bulletin, quoting a copy of a resolution adopted February 13, 1939, by the board of directors of said Association. The resolution is as follows:

> "WHEREAS, Under the 1938 Virginia law the Virginia resident agents are required to be associated with Virginia licensed non-resident brokers in connection with all fire, casualty and surety contracts insuring Virginia risks whether the same be negotiated exclusively by such non-residents or not; and
>
> "WHEREAS The Virginia resident agent is required by said law to be paid at least 50% of the usual commission for same; and
>
> "WHEREAS, Some question has arisen as to the functions and duties of the Virginia resident agent in such cases and this Board has been requested by numerous Virginia agents to define resident agents' duties and functions in such cases,

"NOW THEREFORE BE IT RESOLVED:

"(1) Whenever a Virginia resident agent is requested to countersign such a Virginia coverage contract he shall consider himself associated with the non-resident agent or broker who negotiated same. In all cases where a Virginia agent is associated in the writing of a Virginia policy or contract by a fire, casualty or surety insurance company or a non-resident Virginia licensed broker, the Virginia agent shall, before countersigning the policy or contract, contact the assured or his Virginia representative, if practicable, and familiarize himself with all pertinent facts relating to the policy or contract. Thereupon he shall carefully examine the policy or contract to ascertain whether same is in proper form, correct as to rates and coverage and is best adapted to the proper needs and requirements of the assured. He shall make such suggestions as to any changes therein, as he may deem advisable.

"(2) Throughout the life of any such contract the Virginia resident agent shall be under the same obligations to the assured with respect to servicing the contract as he would be if he alone had negotiated it. Where a Virginia resident agent is associated with the writing of such contract by a Virginia licensed non-resident broker, he shall respect the ownership of the expiration by such non-resident broker as is incorporated in the principles of the American Agency System and when requested by such non-resident broker render his assistance to secure the renewal or continuance of the contract" (R. 279-280).

The foregoing shows, in a general way, what the statute contemplates will be done in Virginia by the resident agents. This will be discussed in more detail later in this brief under Point V.

In addition to what the statute may be said to contemplate that the *agents* will do in Virginia, it also requires the *insurance companies* to do certain things in this State. The company must make every contract negotiated "through" a licensed resident agent; that is, it must associate a resident agent in the transaction. The company must have the contract countersigned by such resident agent and must pay him full commissions, with the proviso that the said agent may pay half of same to a non-resident Virginia licensed broker if said broker negotiated or assisted in the negotiation of the contract. These things the *company* is required to do, but all of them are required to be done *in Virginia*. The statute here challenged does not forbid the company from doing anything outside of the state.

It is clear, therefore, that while the contract may be negotiated *outside the state*, the regulatory provisions are restricted to what shall be done *within the state*, as a result of such outside negotiations. The statutes clearly undertake to regulate the servicing in Virginia of contracts covering risks domiciled there. They are strictly *servicing regulations*.

II.

The Fact that a Virginia Coverage Insurance Contract is Negotiated and Made Outside the State Does Not Impair Virginia's Jurisdiction to Regulate the Insurance Company's Acts and Transactions Performed or to be Performed Within the State in Connection With or Pursuant to Such Contract.

In the very nature of things there should be little doubt about the correctness of the proposition above stated. Insurance companies are as much subject to the regulatory police powers of the state as railroads, power companies, telegraph and telephone companies, or other public

service corporations. It would hardly be contended that a power company, such as the Virginia Electric Power Company, could make in New York a valid contract with the DuPont Company for electric power for that Company's plant near Richmond at rates which would be in violation of those lawfully prescribed by the Virginia State Corporation Commission, or a valid contract for light or power service which would in any manner violate the Commission's lawful regulations, or violate any state law. Nor could a similar contention be plausibly advanced with respect to such a contract for intrastate services of a railroad company, a telephone or telegraph company, a water or gas company, or any company the business of which is clothed with a public interest so as to bring it within the state's regulatory police power.

As said by Mr. Justice Brandeis in *Home Ins. Co.* v. *Dick*, 281 U. S. 407, "A state may, of course, prohibit and declare invalid the making of certain contracts within its borders. Ordinarily it may *prohibit performance* within its borders, even of contracts validly made elsewhere, if they are required to be performed within the state and their performance would violate its laws." Thus, if an insurance contract is made in violation of Virginia laws relating to countersignature, payment of commissions or other valid regulations made pursuant to Virginia statutes, the performance of such contract in Virginia is prohibited by a fine or by revocation of the insurance company's license to do business in the State. In this connection subordinate proposition A will now be discussed.

A. All Casualty and Surety Policies and Contracts Covering Virginia Risks Require or Contemplate Acts of Performance in Virginia.

Copies of the standard contracts in use by appellant companies covering various casualty and surety risks have been filed as exhibits in this case. An examination of them discloses that they all contemplate or require acts of performance in the state which is the situs of the coverage. They will be taken up separately.

Appellants' Exhibit No. 4 (R. 178-184) is a copy of an "Automatic Schedule Fidelity Bond," which indemnifies an employer against loss from certain dishonest, fraudulent or criminal acts of the employee. An examination of same shows the following acts or events occurring in Virginia which would effect the terms of the contract or the performance thereof:

(a) The discontinuance of one or more employees, the addition of one or more employees in the same service, or the transfer of an employee from one of the named positions in the service to another. This liability as to new or transferred employees continues for two months after employment without notice to the company, and thereafter upon notice and acceptance thereof. These new employments and transfers occur in Virginia.

(b) The contract imposes on the assured an obligation to bring legal proceedings against the defrauding employee, or make adjustments and settlements of loss with the employee and receive payment. All such payments operate to reduce the liability of the assured. These acts occur in Virginia.

(c) If the domicile of the assured is in Virginia, the loss would be legally payable in Virginia since the contract does not specify any other place of payment (*Bothwell* v. *Buckbee*, 275 U. S. 278).

(d) Losses would be investigated or adjusted in Virginia.

Appellants' Exhibit No. 5 (R. 185-190), which is a plate glass policy indemnifying the assured against loss or damage by accidental breakage of the glass covered, including lettering and ornamentation, reveals the following acts or events which it is contemplated might or will occur in Virginia:

(a) The assured may notify an authorized Virginia agent of the insurer of a loss, which would be investigated in Virginia.

(b) The broken glass becomes the property of the company, and its agents will take possession of and dispose of same.

(c) The insurer is given the option to pay the loss in money or to replace the glass, lettering and ornamentation. The replacement would necessarily be done in Virginia.

(d) The insurer is given the right to inspect the premises and glass, and may suspend the risk or cancel same pursuant thereto. The inspection would be done in Virginia.

(e) The insurer is subrogated to the insured's rights and claims against any tort feasor for causing the damage. The enforcement of this right would be done in Virginia.

(f) If the insured is domiciled in Virginia, the place of payment of the loss is in Virginia.

Appellants' Exhibit No. 6 (R. 178, 191-196) is a copy of the standard auto liability fleet policy, indemnifying

the assured against liability for bodily injury or property damage resulting from the operation of the motor vehicles covered. It contemplates the following acts or performances on the part of the insurer in Virginia:

(a) The insurer obligates itself to defend all suits against the assured for damages resulting from the operation of the vehicles. Where the accident occurs in Virginia the suit would be in Virginia.

(b) The insurer is given the right to make such investigation of accidents and such settlement of claims against the assured as it sees fit. This would be done in Virginia.

(c) The insurer agrees to pay premiums on bonds to release attachments, and premiums on appeal bonds. These payments would be made in Virginia.

(d) The insurer agrees to pay on behalf of the insured all sums and discharge all liability insured against, for which the assured is legally liable. These payments would be made in Virginia.

(e) The insurer automatically becomes liable for losses sustained by reason of the operation of newly acquired motor vehicles, these being automatically added to the coverage, and the insurer automatically becomes liable for the payment of any additional premiums therefor. The acquisition of these new vehicles would occur in Virginia.

(f) The assured may notify any authorized Virginia agent of the insurer of accidents arising from the operation of the vehicles.

(g) Upon the death or bankruptcy of the assured, the policy automatically becomes transferred for a period of thirty days to the assured's legal successor. This transfer may occur in Virginia.

(h) The insurer is subrogated to all of the assured's rights of recovery against third persons. These rights would be enforced in Virginia.

(i) If the domicile of the assured is in Virginia, the insurer is obligated to pay the loss in Virginia.

Appellants' Exhibit No. 7 (R. 178, 197-200) is a copy of the standard accident policy. The evidence shows this policy is rarely issued to a person other than one domiciled in the state of the situs of the risk. It contemplates payment of the loss, which includes in some cases the payment of certain weekly indemnities. These payments would be made in Virginia usually. It is obvious that this contract contemplates an investigation of the facts in Virginia by the insurer pertaining to any claim for disability or accident to determine the *bona fides* of the claim and to escape the payment of fraudulent claims.

The appellants' Exhibit No. C (R. 494-505) is a copy of the standard workmen's compensation policy in use by The Travelers Insurance Company, and is substantially the same as those in use by other companies. This contract indemnifies the insured against liability to employees under the workmen's compensation law, and contemplates performance in Virginia by the following acts:

(a) The payment to the employee of any amount he becomes entitled to receive by reason of the workmen's compensation laws. Almost invariably the employee is

domiciled in Virginia and the payment to him would be made here.

(b) *The rendering of service to the employer or assured*: (1) by the inspection of the work places in Virginia covered by the policy; (2) by making suggestions to the assured as to changes or improvements to reduce the number or severity of injuries; (3) the investigation of and settlement of claims.

(c) Defending in the name of and on behalf of the assured, all suits or legal proceedings growing out of any such injuries, whether or not the suits be groundless, false, or fraudulent. These suits would be tried in Virginia.

(d) The payment of all costs taxed against the assured in any such suits and all expenses incurred by the insurer for investigation, negotiation or defense of such suits. These payments would be made in Virginia.

(e) The New York Branch Manager Nicholls (114 to 118) testified that it is customary to issue blanket workmen's compensation policies which become effective and protect the insured, without notice to the insurer, immediately upon the beginning of a new activity in any one of the United States. The mere beginning of the construction of a building by a contractor in Virginia would automatically operate to bring the assured within the protection of the contract. The legal effect of this is that the contract itself is made in Virginia (*Palmetto Ins. Co.* v. *Conn*, 272 U. S. 295, 77 L. ed. 243).

(f) The inspection by the insurer of the plants, works, machinery and appliances of the assured in Virginia.

(g) An examination by the insurer of the books of the insured so far as they relate to the remuneration earned by the employees in order to determine the amount of the premium or other relevant matters.

(h) The contract declares the obligation to be a direct one from the insurer to any injured employee, or, in the event of his death, to his dependents, and enforceable against the insurer by such employee or dependent without regard to any default of notice or payment of premiums on the part of the assured. This enforcement would occur in Virginia.

(i) The insurer is subrogated, as to all payments made to, or rights of recovery therefor vested by law in, the assured or any employee or dependent of such employee, against third persons, corporations, associations, or estates. This right of subrogation would be enforced in Virginia.

(j) There are other miscellaneous provisions in the policy, such as notices to agents which would occur in Virginia, but the foregoing are sufficient to demonstrate that a contract of this kind contemplates very many acts in Virginia on the part of the insurer.

It is unnecessary to go into further detail with respect to the various acts of performance or other acts which it is contemplated will take place in Virginia in connection with the obligations incurred by the insurer under the many types of contracts covering Virginia risks, but the foregoing are fairly illustrative of them all.

As to the services customarily performed in Virginia by the inspectors and engineers of the insurers, the testimony of the appellant Adair, who is the Richmond Branch Manager of the Fidelity and Casualty Company,

also one of the appellants, contains a concise and detailed statement with respect to the different types of service which it is customary for the appellant companies to render in connection with their policies and contracts (R. 240). This witness testified that no distinction is made as to services rendered by the inspectors, engineers and claim adjusters in connection with a policy or contract negotiated outside the State from those rendered where a similar contract is negotiated in Virginia (R. 243). He testified that in mechanical lines "A considerably larger load of the premium goes for inspection and engineering than for the payment of losses. It is really servicing insurance with a guarantee back of it that if our inspection and engineering services don't prevent the loss, we will pay for it" (R. 241).

The nature of the services rendered, as stated by this witness, is elaborated in greater detail by the appellants' witness Murphy (R. 713, *et seq.*), who is the chief of the engineering and inspection service of The Travelers Insurance Company in Virginia. In fact it is not disputed in the record that the investigation and engineering service customarily rendered by casualty and surety companies in Virginia, with respect to contracts negotiated outside of the State, is very extensive, and that all loss claims in connection with such contracts are customarily handled through the claim division or the claim adjuster of the insurance company in Virginia. In fact, appellants have taken the position that, by reason of the efficient, complete, and extensive services rendered by the insurer's inspectors, engineers, and claim adjusters in Virginia, in connection with such contracts, the necessity for the services of the local resident impartial agent is dispensed with.

B. The Making Outside of Virginia of an Insurance Contract Which Contemplates or Requires the Doing by the Insurance Company of Acts in Virginia, Constitutes, as a Matter of Law, an Exercise of the Insurance Company's License, Right, Franchise, or Privilege, of Doing an Insurance Business in Virginia.

We are not here concerned with the question whether acts of *negotiation* done outside of the State concerning the making of a Virginia coverage contract, whether successful or unsuccessful, would be so intimately connected with the exercise of the insurance company's state license privilege to be actually a part of same. The statute here challenged does not regulate such negotiations, and therefore the question is not involved. But it has been well established for many years that the *making* of such a contract is an exercise of such privilege.

The case of *Bothwell v. Buckbee, Mears Co.*, 275 U. S. 274, 72 L. ed. 277 directly decided this question. A mutual insurance company, not licensed in Minnesota, had made in Maryland a strike insurance contract to indemnify the assured against strike losses which would occur at the assured's plant in Minnesota. It does not appear that any strike occurred or that any losses were sustained, but suit was brought in Minnesota to compel the assured to pay the assessment made against it by the mutual company. The assured defended on the ground the insurance company, not being licensed to do business in Minnesota, should be denied the right to enforce same in its courts. The insurer's agents had solicited the contract in Minnesota, and this court held that this activity was doing business in the state in violation of its laws. But the court went further and held that it was also in violation of the laws of that state for an insurance company, unlicensed in Minnesota, to make in Maryland a contract which contemplated acts of per-

formance in Minnesota. In pointing out the various acts which the contract contemplated would be performed in Minnesota and which had the effect of violating its laws relating to the admission of foreign insurance companies to the state, Mr. Justice Brandeis said:

> "But the contract was also in its terms obnoxious to the Minnesota law. It required the company to perform, in Minnesota, acts which it was prohibited from doing there. The company agreed to defend, on behalf of the insured, any suits or other legal proceedings brought by striking employees against the insured to enforce claims arising out of any strike, and to pay any expenses incurred by the company in so doing. This covenant necessarily involved performance in Minnesota, as suits against the insured would be brought in that state, among other reasons, because it was a Minnesota corporation and had no place of business elsewhere. The company also covenanted to indemnify the insured for 'direct loss of average daily net profits and fixed charges,' due to strikes. The contract did not specify the place where payment for the loss should be made, so that under the common rule the insurer would be required to make the payment in Minnesota, the domicile of the insured. *Pennsylvania Lumbermen's Mut. F. Ins. Co.* v. *Meyer*, 197 U. S. 407, 416, 41 L. ed. 810, 815, 25 Sup. Ct. Rep. 483.
>
> "Besides these acts which the company bound itself to perform in Minnesota, the contract reserved to it the right to do, in Minnesota, and the company contemplated doing there, other acts forbidden by its laws, namely, the right to inspect the plant and the books of account and papers of the business; and the right to interrogate persons connected with it. Moreover, the contract clearly contemplates that not only these examinations, but the appraisals and other acts provided to be done by the company in the course

of the adjustment of losses, shall be done in Minnesota. All these things were activities of the insurance business which the company was prohibited by valid statutes from doing within the state. *Pennsylvania Lumbermen's Mut. F. Ins. Co.* v. *Meyer, supra*, pp. 414, 415. Compare *Commercial Mut. Acci. Co.* v. *Davis*, 213 U. S. 245, 256, 53 L. ed. 782, 787, 29 Sup. Ct. Rep. 445. Under rules of law generally applicable a state may refuse to enforce a contract which provides for doing within it an act prohibited by its laws. * * *" (275 U. S. at page 277; 72 L. ed. at page 280).

It follows that if the making of such a contract outside the state by a company *not licensed* in the state is *unlawful* because of the *want of a license*, and if the making of such a contract by a *licensed* company is *lawful* because of the *possession of a license*, then the making of the contract is necessarily an exercise of the franchise or privilege *granted by the license*. After detailing the various acts of performance which the insurance contract required to be done in Minnesota (which have been quoted above), the opinion continued:

"A contract of insurance, although made with a corporation having its office in a state other than that in which the insured resides and in which the interest insured is located, is not interstate commerce. *New York Life Ins. Co.* v. *Deer Lodge County*, 231 U. S. 495, 58 L. ed. 332, 34 Sup. Ct. Rep. 167; *National Union F. Ins. Co.* v. *Wanberg*, 260 U. S. 71, 75, 67 L. ed. 136, 138, 43 Sup. Ct. Rep. 32. Hence Minnesota had the power to prohibit the Employers' Mutual Company from doing business within the state without first complying with the prescribed conditions; and could refuse the aid of its courts in enforcing a contract which in-

volved violation of its laws. * * *" 72 L. ed. 277, 279).

About two weeks before the decision in the above case (*Bothwell* v. *Buckbee*) this Court had rendered its decision in the case of *Compania General de Tabacos de Filipines* v. *Collector of Internal Revenue,* 275 U. S. 87, 72 L. ed. 177. This case involved the validity of two separate taxes assessed by the Philippine Islands upon insurance premiums payable under two separate contracts of insurance. The taxing statute imposed the tax directly upon the assured, but the court, in deciding the question of its validity, treated it as, in effect, a tax upon the insurance company, saying, "We may properly assume that this tax, paid by the assured, must ultimately be paid by the insurer; and treating its real incidence as such, the question arises * * *." The court also held that the validity of the statute was to be determined by the application of the same principles of due process and equal protection as if the Philippine Islands were a state.

The tax on one of these contracts was held to be within the constitutional jurisdiction of the Philippines to impose, while the tax on the other contract was held beyond its jurisdiction. The distinction between the two insurance contracts is most illuminating upon the question of what constitutes the exercise by a foreign insurance company of its privilege of doing business in a state under its license. The assured was a foreign tobacco corporation licensed to do a local business in the Philippines. One of the insurance companies (referred to as the London Company) was also licensed, while the other (the Paris Company) was not. Both contracts were negotiated and made outside the Philippines. Losses were

payable in London and Paris, respectively. The court held that since the Paris Insurance Company was not licensed in the Philippines, the Islands had no jurisdiction over the transaction and therefore could not tax same. But as to the London Insurance Company's policy insuring against loss by fire of goods in the Philippine warehouses of the assured, the court said that the question presented was "whether making and carrying out the policy does not involve an exercise or use of the right of the London Company to do business in the Philippine Islands under its license, because the policy covers fire risks on property within the Philippine Islands which may require adjustment and the activities of agents in the Philippine Islands with respect to settlement of losses arising thereunder. This we think must be answered affirmatively * * *."

Thus the court held that the sole fact that losses *might* arise which *might* contemplate adjustment and activities of the insurer's agents in the place of coverage was alone sufficient to require the conclusion that the making of the contract was an exercise or use of the right or privilege of the insurance company to do a local business under its license. While there are other cases which might be discussed, such as *Pennsylvania Lumbermen's Mutual F. Ins. Co.* v. *Meyer,* 197 U. S. 407, 41 L. ed. 810, and *Equitable Life Insurance Society* v. *Pennsylvania,* 238 U. S. 143, 59 L. ed. 1230, which is quoted from at length in the opinion below, it is not deemed necessary to thus burden the Court. The undisputed evidence in this case shows (see II-A *supra*) not only the necessity for, but the customary doing of many and various acts in Virginia by the insurance companies' engineers and inspectors in connection with these contracts made outside the State,

in addition to the activities of the claim adjusters in settling claims arising thereunder, referred to in the Philippine Tobacco case.

There can be no escape, therefore, from the conclusion that when one of the appellant companies makes a contract of surety or casualty insurance outside of Virginia but covering a risk, the situs of which is in Virginia, then the making of such contract contemplates, calls for, or permits acts of performance in Virginia, and involves an exercise or use of the company's right or privilege of doing business in Virginia under the license granted by the State.

C. The Making Outside of Virginia of a Contract of Insurance Involving an Exercise of a Foreign Insurance Company's License, Right or Privilege of Doing Business in Virginia, Brings the Contract Within the Jurisdiction and Regulatory Police Power of Virginia.

The above statement involves the ultimate or fundamental issue with respect to the question of jurisdiction to regulate. The appellants contend that even though the exercise of the Virginia license privilege in making an insurance contract confers jurisdiction to *tax* the contract, it does not follow that it likewise confers jurisdiction to *regulate* the carrying out or performance of the contract. This identical question came up in the *Compania Gen. Tabacos Case, supra,* which it has just been shown (B, *supra*), establishes the principle that the making of the contract is an exercise of the license privilege. As will be recalled, it involved the validity of a tax imposed by the Philippine Islands on the assured with respect to two insurance contracts made in Europe, one with a licensed insurance company and the other with an unlicensed one. The entire court was in accord that there was jurisdiction to tax the contract made with

the licensed insurance company because the contract was made in the exercise of said insurance company's license privilege. But Justice Holmes and Brandeis dissented from the court's decision that there was no jurisdiction to tax the assured with respect to the contract with the *unlicensed* insurance company. They thought the case should be distinguished from the *Allgeyer* (165 U. S. 578) and *St. Louis Cotton Compress* (260 U. S. 346) cases on the ground of "the difference between a penalty and a tax." But the majority of the court refused to recognize any distinction in so far as a state's jurisdiction is concerned, recognizing the principle that if a state has jurisdiction at all over a transaction, it has jurisdiction to regulate as well as to tax. Mr. Chief Justice Taft, in the court's opinion, pointed out that it was true that the fine and penalty in the *Allgeyer* and *St. Louis Compress* cases were intended as regulatory measures to discourage insuring in nonadmitted insurance companies, but the Chief Justice said, referring to the Philippine tax on the assured:

> "* * * And that is just what this tax is for. Even though it is only equal to the tax upon normal premiums paid in the Philippine Islands, it is imposed *for the purpose of discouraging insurance* in companies that do not pay tribute to the state because out of its taxing or penalizing jurisdiction. As the language above quoted from the opinion in the *St. Louis Cotton Compress Co. Case* shows, the action of Arkansas was invalid, *because of its attempt 'to regulate' the conduct of the Compress Company in respect to a matter not within its local jurisdiction. Taxation is regulation just as prohibition is.*" (Italics supplied. 72 L. ed. 177, 181.)

And the court also said in this connection:

> "* * * We are unable to see any sound distinction between the imposition of a so-called tax and the imposition of a fine in such a case. A so-called tax is just as much an interference with the liberty of contract as is a penalty by fine, where the subject matter giving rise to the imposition is beyond the jurisdiction of the state. * * *" (*Id.*)

But though the court held that the Philippines could not regulate by means of the tax the contract made in Europe between the assured and the *unlicensed insurance company,* it distinctly held that the Philippines *did possess the power to regulate by such a tax* the contract similarly made between the assured and *the licensed insurance company.* As to this contract the Chief Justice said:

> "We come now to the question of the tax upon the premiums paid to the London Company, which was licensed and presumably was doing business in the Philippine Islands. Does the fact that while the Tobacco Company and the London Company were within the jurisdiction of the Philippines they made a contract outside of the Philippines for the insurance of merchandise in the Philippines, prevent the imposition upon the assured of a tax of 1 per cent upon the money paid by it as a premium to the London Company? We may properly assume that this tax placed upon the assured must ultimately be paid by the insurer, and treating its real incidence as such, the question arises whether making and carrying out the policy does not involve an exercise or use of the right of the London Company to do business in the Philippine Islands under its license; because the policy covers fire risks on property within the Philippine Islands which may require adjustment

and the activities of agents in the Philippine Islands with respect to settlement of losses arising thereunder. This we think must be answered affirmatively under *Equitable Life Assur. Soc.* v. *Pennsylvania*, 238 U. S. 143, 59 L. ed. 1239, 35 Sup. Ct. Rep. 829. The case is a close one, but in deference to the conclusion we reached in the latter case, we affirm the judgment of the court below in respect to the tax upon the premium paid to the London Company" (72 L. ed. 177, 182, 183).

This case clearly and unmistakably upholds the jurisdiction of the state, both to tax and to regulate the acts outside the state of a foreign corporation where such acts are done *in the exercise of the corporation's license privileges*. If the Tabacos Company's contract with the unlicensed Paris Company had been made *in the exercise of the Tabacos Company's license privilege*, the state would have had jurisdiction to tax it. It did have jurisdiction to tax the licensed London Company contract because it was made in the *"exercise or use of the right* of the London Company to do business in the Philippines *under its license."* The privileges conferred on a *manufacturing* company by its license to do business in the state are essentially different from those conferred by a license to do an *insurance* business. Furthermore, the former is not, while the latter is, clothed with a public interest and subject to a greater degree of regulation.

In *Great A. & P. Tea Co.* v. *Grosjean*, 301 U. S. 412, the identity in principle of a state's jurisdiction to tax with its jurisdiction to exercise its regulatory police power is emphasized. The case involved the validity of a Louisiana statute imposing license taxes on chain stores. The amount of the tax on each store was graduated or measured by the number of stores operated by the licensee

in the entire United States. The A. & P. Company operated over fifteen thousand stores in the various states but only 106 in Louisiana, and the tax on each of its Louisiana stores was $550.00. Another licensee operated 92 stores all in Louisiana and the tax on each of its stores was $30.00. The statute was challenged as violative of due process because allegedly it was, in effect, a tax upon stores located outside the state. The court, however, held it valid as a regulatory measure, and in effect an exercise of the police power through the medium of taxation. Mr. Justice Roberts, speaking for the court, said:

> "Our decision need not, however, rest on conceptions of subject, measure and rate of tax. Much broader considerations touching the state's internal policy of police sustain the exaction. The tax is laid solely upon intrastate commerce. In the exercise of its police power the state may forbid, as inimical to the public welfare, the prosecution of a particular type of business, or regulate a business in such manner as to abate evils deemed to arise from its pursuit. Whatever a state may forbid or regulate it may permit upon condition that a fee be paid in return for the privilege, and such a fee may be exacted to discourage the prosecution of a business or to adjust competitive or economic inequalities. Taxation may be made the implement of the exercise of the state's police power; and proper and reasonable discrimination between classes to promote fair competitive conditions and to equalize economic advantages is therefore lawful" (81 L. ed. 1193, 1201).

Upon principle it is difficult to perceive any theory upon which any possible distinction can be drawn between a state's *jurisdiction* to exercise its taxing power and its

jurisdiction to exercise its police power or any other proper governmental power. The Constitution certainly contains no provision which can be made the basis for any distinction. The Tenth Amendment provides that "the powers not delegated to the United States by the Constitution, nor prohibited by it to the states are reserved to the states, respectively, or to the people." Of course, if the state has no jurisdiction over a transaction, it may neither tax nor regulate it, but if it does have jurisdiction, it necessarily follows that it may do both. Not only does the Constitution make no provision for cases in which a state's taxing jurisdiction may exist but where its jurisdiction to exercise the police power does not exist, but I have been able to find no decision of this Court or any other court which recognizes any such distinction. On the contrary, this Supreme Court in the *Philippine Island Tobacco Case, supra* (275 U. S. at p. 95) said:

> "We are unable to see *any sound distinction* between the imposition of a so-called tax and the imposition of a fine in such a case. A so-called tax is just as much an interference with the liberty of contract as is a penalty by fine, *where the subject matter giving rise to the imposition is beyond the jurisdiction of the state.*" (Italics supplied.)

Of course, the imposition of a fine is necessarily an exercise of the regulatory police power, while a tax may or may not be such an exercise.

It follows as a necessary conclusion, therefore, from what has been said under subheads A, B and C, *supra*, that the second proposition is unquestionably supported by the evidence and the decisions of this Court, and that

Virginia has jurisdiction to regulate the performance in this State of all Virginia coverage casualty and surety contracts negotiated or made outside of the state.

III.

Virginia May Prohibit the Doing in Virginia by an Insurance Company Licensee of Any Act in Connection With or in the Performance of a Virginia Coverage Contract Made by it Outside the State in Violation of Virginia Laws, by the Imposition of a Fine or by Revocation of Said Company's License to do Business in the State.

Section 4231 of the Code of Virginia provides that any insurance company violating any provision of the statute here challenged shall be fined not less than ten dollars nor more than one thousand dollars for each offense.

The State's jurisdiction to impose this fine is clearly established by the decisions of the Supreme Court which have just been discussed, holding that the jurisdiction to fine is co-extensive with the power to tax. (II-C, *supra*.)

Section 4180 of said Code empowers the State Corporation Commission to suspend or revoke the license of any insurance company "which fails or refuses to perform any lawful requirements imposed by the laws of this state." See also Section 4223 of the Code.

The action of the State in revoking a license to do business in the State, is, like a fine, an exercise of the police power. That it is a proper exercise of such power is well established. In *Hanover Fire Ins. Co.* v. *Carr*, 272 U. S. at p. 515, 71 L. ed. at p. 382, Mr. Chief Justice Taft thus stated the doctrine:

> "* * * The state in dealing with foreign corporations may properly and without discrimination as between them and domestic companies regulate

> the former by a provision that for a failure by them to comply with any valid law governing the conduct of their business in the state the license already granted may be revoked. That is a legitimate condition in the treatment of foreign companies which do not have property and home within the state. It is a police regulation. * * *"

The revocation of the license to do business in the state being, like the imposition of a fine, an exercise of the police power, the state's jurisdiction to do the one is conclusive of jurisdiction to likewise do the other.

The effect of the statute, as applied to Virginia contracts made outside the State, is to require insurance companies to exercise their license privileges, at least in doing in Virginia acts in performance thereof, in such manner as to conform to the requirements of the laws of the State. An illustration of an appropriate application of this statute would be to revoke the license of an insurance company which would persist in making workmen's compensation or fleet automobile liability insurance contracts outside the State in violation of the prescribed Virginia rates. It might be contended that there is no violation of this law in Virginia until there has been payment of a loss under the contract. But under the decisions hereinbefore cited the company is doing business in the State under its license when it inspects the machinery or automobiles, or holds safety meetings, adjusts claims or otherwise services the contracts. In fact, many proposed risks are examined or inspected in the State and reports made *before* the insurance company determines whether it will make the proposed contract or issue the policy. Likewise, should an insurance company licensee make outside the State a similar contract

without procuring the countersignature of a Virginia resident agent or without paying to such agent the commissions required by the statute, and should it have its inspectors, engineers or claim adjusters perform any act in Virginia in connection with or pursuant to such contract, such company would become liable to fine or to revocation of its license. The only legal way the company can perform such a contract in Virginia is to associate therewith, in the manner above stated, a local resident Virginia agent. If it should attempt to perform the contract without such association it would clearly violate Virginia laws. *Bothwell* v. *Buckbee, supra.*

As said in *Home Ins. Co.* v. *Dick,* 281 U. S. 407:

> "Ordinarily, it (a state) may prohibit performance within its borders, even of contracts validly made elsewhere, if they are required to be performed within the state and their performance would violate its laws."

IV.

The Fact that a Virginia Coverage Contract, Made by an Insurance Company Licensee in Violation of Virginia Laws, is Made Outside the State Does Not Impair the Jurisdiction of Virginia to Revoke the Company's License to do Business in the State Because of MAKING Such Contract in Violation of Her Laws.

It has been heretofore shown that every Virginia coverage casualty or surety contract, though made outside the State, contemplates and permits the doing of acts in Virginia, and that the making of the contract is itself an exercise of the insurance company's license privilege of doing business in the State (11-B, *supra*).

It has also been shown that the State may fine or revoke the license of such a company for *the doing of any acts in Virginia* in connection with or in performance of any such contract made outside the State in violation of her laws.

The fourth proposition above stated is that the *making* of the contract in such manner as to violate the legal requirements of the State subjects the insurance company to revocation of its license; that the making of the contract, without obtaining the required countersignature and associating therewith the Virginia agent by paying him the required commissions, *without doing any act inside the State*, subjects the company to such revocation.

While the jurisdiction of the State to revoke the license for *acts done in the State* pursuant to such a contract is sufficient to support the validity of the statute, it can be more effectually enforced if such revocation may be had solely because of the *making* of such a contract without complying with Virginia laws.

The evidence clearly shows that persons negotiating insurance contracts attach a great deal of importance to the fact that the insurer is licensed to do business in the state of coverage. The appellant's witness Nicholls admitted that it is an advantage to the assured to be able to bring suit in the state where the loss occurs (R. 153). This is an obvious truth, because the witnesses to the event causing the loss live in the state of coverage, and it would cause great inconvenience and expense to transport them to some other state where process may be lawfully executed. Appellants' witness Thomas, a New York broker, testified that he never places his clients' risks in companies not admitted to the state where the risk is located; that he and his associates did not "want

insurance companies that are only entered in a few states. *We want complete service wherever we need it"* (R. 812). Since the making of the contract contemplates that the insurance company's engineers, inspectors and claim adjusters will render service in connection therewith in the state of the situs of the risk, it is necessarily true that a nonadmitted company could not legally carry out the contract, and would prove entirely unsatisfactory. *Bothwell* v. *Buckbee, supra.* Another of appellants' witnesses, Otis, also a New York broker, testified that as to a fleet automobile risk "or a risk that is domiciled in Virginia, obviously they have to service it, and in those cases we are always certain of having a company on the risk that is entered to do business in that state." He was then asked the question: "Would you place a risk of that kind in a nonadmitted company?" To which he replied: "Not a risk that is domiciled in the state" (R. 876).

Thus the insurance company is clearly using its Virginia license privilege as an inducement to assureds to contract with it. Suppose, without disclosing the fact to the assured, it makes the contract in violation of Virginia laws so as to incapacitate itself from legally rendering this service in Virginia. Obviously this operates as a fraud upon the assured; for which the insurer could be made to respond in damages. See section 360, comment b. Restatement of the Law, Conflict of Laws. It would be an anomalous situation, indeed, if Virginia were helpless to prevent such a flagrant abuse of the license privileges granted by her.

It seems clear that, in a proceeding in Virginia to declare the forfeiture of the insurance company's license in such a case, it could not be heard to say that it did not

perform its obligations contemplated by the contract, or did not intend to perform same. The mere fact that the act of making the contract takes place in New York does not, in any sense, remove it from the effect of the Virginia statutory provisions prescribing the terms under which it must exercise its license privilege. This is well illustrated in the case of *Bradford Electric Company* v. *Clapper*, 286 U. S. 145, 76 L. ed. 1027, which involved the right of an employee to sue his employer for personal injuries sustained through the employer's negligence. The contract of employment was made in Connecticut. The statutes of that state provided compensation payments for injuries but denied the right to sue for damages. The employee was temporarily working in *New Hampshire*, whose laws permitted such action, and there sustained the injuries. He brought an action for damages in the United States District Court of New Hampshire and the defense was that, the employment having been made in Connecticut, the laws of that state which prohibited such actions controlled the rights of the parties, and that these rights were not affected by the fact that *the act which caused the injury was done in New Hampshire*. In sustaining this ground of defense and in holding that laws of Connecticut controlled the legal consequence of the defendant's act done in New Hampshire, Mr. Justice Brandeis said:

> "The administratrix contends that the full faith and credit clause is not applicable. The argument is that to recognize the Vermont Act as a defense to the New Hampshire action *would be to give to that statute an extra-territorial effect, whereas a State's power to legislate is limited to its own territory*. It is true that full faith and credit is enjoined

by the Constitution only in respect to those public acts which are within the *legislative jurisdiction* of the enacting State. See *National Mut. Bldg. & L. Assn.* v. *Brahan*, 193 U. S. 635, 647, 48 L. ed. 823, 828, 24 S. Ct. 532; *Olmsted* v. *Olmsted*, 216 U. S. 386, 395, 54 L. ed. 530, 533, 25 L. R. A. (N. S.) 1292, 30 S. Ct. 292. But, obviously, *the power of Vermont to effect legal consequences by legislation is not limited strictly to occurrences within its boundaries.* It has power through its own tribunals to grant compensation to local employees, locally employed, for injuries received *outside its borders*, compare *Quong Ham Wah Co.* v. *Industrial Acci. Commission*, 255 U. S. 445, 65 L. ed. 723, 41 S. Ct. 373, dismissing writ of error, 184 Cal. 26, 12 A. L. R. 1190, 192 Pac. 1021, and likewise has power to exclude from its own courts proceedings for any other form of relief for such injuries.

* * * * *

"The answer is that such recognition in New Hampshire of the rights created by the Vermont Act, can not, in any proper sense, be termed an extraterritorial application of that Act. Workmen's compensation acts are treated, almost universally, as creating a statutory relation between the parties—not, like employer's liability acts, as substituting a statutory tort for a common law tort. [citing authorities.] The relation between Leon Clapper and the Company was created by the law of Vermont; *and as long as that relation persisted its incidents were properly subject to regulation there.* * * *." (76 L. ed. 1033, 1034. Italics supplied.)

Paraphrasing the last sentence quoted it may with equal truth be said, in so far as the question of jurisdiction is concerned, that the relation between Virginia and the licensee company was created by the laws of Virginia and

as long as that relation persisted incidents to the use of the license privilege, such as making a Virginia coverage contract, are properly subject to regulation wherever the contract is made. The fact that the contract is made in New York no more strips Virginia of jurisdiction to take legal cognizance of same than the fact that the employee was injured in New Hampshire deprived Connecticut of the power to fix the legal consequences of his injury.

Another case which is especially enlightening on this precise question of the jurisdiction of a state to legislate with respect to practices and acts of its licensees which take place outside the state is the Louisiana chain store case, *Great A. & P. Tea Co.* v. *Grosjean, supra*, in which was challenged the validity of a chain store tax, the amount of the tax on each store *being determined by the entire number of stores operated by the licensee in the United States*. The A. & P. Company contended that it was beyond the jurisdiction of Louisiana to give legislative effect to that company's operations in other states. Said the court, "the claim is, essentially, that even if local evils flow from the appellant's methods the state cannot control those evils because its power is limited to conditions created by the members of the chain found within the state." The court said further, in answer thereto:

> "* * * The policy Louisiana is free to adopt with respect to the business activities of her own citizens she may apply to the citizens of other states who conduct the same business within her borders, *and this irrespective of whether the evils requiring regulation arise solely from operations in Louisiana or are in part the result of extra-state transactions.* It is not a denial of due process to adjust such license taxes as are here involved to meet the local evil

resulting from business practices and superior economic power even though those advantages and that power are largely due to the fact that the taxpayer does business not only in Louisiana but in other states." (81 L. ed. 1202. Italics supplied.)

The Court's attention is again directed to the fact that the above case also held that this tax was an exercise of the state's regulatory police power; also attention is directed to the Philippines Tobacco case which sustained the state's jurisdiction to tax the mere making outside of the state of an insurance contract covering a fire risk located in the state, though the insurance company actually did no act in the state in connection with same, the court saying in the Tobacco case that *that particular tax was intended as a regulatory measure.*

Connecticut Gen. L. Ins. Co. v. *Johnson,* 303 U. S. 77, 82 L. ed. 672, involved the jurisdiction of a state to tax a reinsurance contract made outside the state. The court reaffirmed the doctrine laid down in the Philippines Tobacco case that the state's jurisdiction to tax an insurance contract made outside its borders *is to be determined by whether the contract was made in the exercise of the insurance company's license privilege.* The court said that "the writing of policies without the state insuring residents and risks within it is taxable because within the granted privilege," citing the Philippines Tobacco case. And the court said further, in denying the state's jurisdiction:

"But the limits of the state's legislative jurisdiction to tax, prescribed by the Fourteenth Amendment, are to be ascertained by reference to the incidence of the tax upon its objects rather than the ultimate thrust of the economic benefits and burdens

> of transactions within the state. As a matter of convenience and certainty, and to secure a practically just operation of the constitutional prohibition, *we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it.* Hence it is that a state which controls the property and activities within its boundaries of a foreign corporation admitted to do business there may tax them. But the due process clause denies to the state power *to tax* or regulate *the corporation's* property and *activities elsewhere.*" (82 L. ed. 677. Italics supplied).

This statement can be reconciled with the power of the state to tax the contract made outside its borders but insuring risks therein only upon the principle that the place of making the contract is immaterial, *provided it is made in the exercise of the granted privilege.* The court expressly says in the above quotation that the state cannot tax an object (contract) which it cannot control, and that the power to control is the test of the power to tax. It therefore follows, as a necessary conclusion, that the adjudicated power of the state to *tax* the contract carries with it an adjudication that the state possesses the power to control it. If the state did not have the power to control and regulate the making of the contract, then the state *could not tax it* under the test laid down in this case.

Clearly Virginia has jurisdiction and power to regulate the making outside the State of Virginia coverage contracts by its insurance company licensees. Of course this regulation must be a constitutional one, in the sense that it must not be arbitrary or capricious, and this question will be next considered.

V.

The Objects and Purposes Sought to be Attained by the Challenged Legislation are Legitimate and Proper, and the Means Employed to that End are Not Arbitrary or Capricious But are Reasonable and Appropriately Adapted Thereto.

The statute here challenged involves an exercise of the regulatory *police power* of the state. *German Alliance Ins. Co.* v. *Lewis,* 233 U. S. 389. It may not be inappropriate, therefore, at this time to refresh the memory of the Court by calling attention to a few well known elementary principles relating to its exercise. While the police power is not susceptible of accurate definition, yet it is "one of the most essential of powers, at times the most insistent, and always one of the least limitable." *District of Columbia* v. *Brooke,* 214 U. S. 138. It extends, "not only to regulations which promote the public health, morals and safety, but to those which promote the public convenience or the *general prosperity.*" (Italics supplied.) *Eubank* v. *Richmond,* 226 U. S. 137. As said by Judge Prentiss in *City of Richmond* v. *C. & P. Tel. Co.,* 127 Va. 632: "In the police power, which cannot be surrendered, * * * but which, except as restrained by constitutional inhibition, is unlimited, is found the inexhaustible source of those new legislative regulations which, in response to the needs of a progressive civilization, are designed to promote the public convenience and *general prosperity.*" (Italics supplied.)

As to the legal effect of an apparent deprivation of rights guaranteed under the fourteenth amendment, particularly due process and equal protection, by a state's exercise of its police power, the rule is thus stated in 11 Am. Jur. 995-7:

> "In accordance with the settled principle that no part of the Federal Constitution was intended to hamper a valid exercise of state police regulation, it is particularly established by overwhelming authority that the Fourteenth Amendment was not designed to interfere with, and does not interfere with, curtail, restrain, destroy, or take from the states the right duly and properly to exercise the police power. * * *"

In support of the text numerous decisions of this Court are cited.

In *Mutual Loan Co.* v. *Martell*, 222 U. S. 225, Mr. Justice McKenna thus defined the police power and stated the test to be applied to determine the validity of its exercise by the state:

> "This court has had many occasions to define, in general terms, the police power, and to give particularity to the definitions by special applications. In *Chicago, B. & Q. R. Co.* v. *Illinois*, 200 U. S. 561, 592, it was said that 'the police power of a state embraces regulations designed to promote the public convenience or the *general prosperity*, as well as regulations designed to promote the public health, the public morals, or the public safety'; and that the validity of a police regulation 'must depend upon the circumstances of each case and the character of the regulation, whether arbitrary or reasonable, and whether really designed to accomplish a legitimate public purpose'." (222 U. S. 232. Italics supplied.)

It is, of course, well settled that the state's exercise of its regulatory police power must be a reasonable one and not arbitrary or capricious. The test of what is reasonable, however, depends upon the facts and circumstances

to which each exercise of the power is to be applied. A recent decision of this Court in a case somewhat similar to this furnishes a most instructive precedent. *O'Gorman & Young* v. *Hartford F. Ins. Co.*, 282 U. S. 251, involved the validity of a New Jersey statute which provided that commissions paid by fire insurance companies to their agents should be "reasonable." The agent plaintiffs in that case had a contract entitling them to be paid 25% commissions, but the lower courts found that 20% was the prevailing rate and therefore the contract rate could not be collected. In his opinion, Mr. Justice Brandeis said:

> "The statute here questioned deals with a subject clearly within the scope of the police power. We are asked to declare it void on the ground that the specific method of regulation prescribed is unreasonable and hence deprives the plaintiff of due process of law. As underlying questions of fact may condition the constitutionality of legislation of this character, *the presumption of constitutionality must prevail in the absence of some factual foundation of record for overthrowing the statute. It does not appear* upon the face of the statute, or from any facts of which the court must take judicial notice, *that in New Jersey evils did not exist in the business of fire insurance for which this statutory provision was an appropriate remedy.* The action of the legislature and of the highest court of the state indicates that such evils did exist. The record is barren of any allegation of fact tending to show unreasonableness." (282 U. S. 257-8. Italics supplied.)

Thus, the case holds, in effect, that the burden rests on him who challenges the exercise of the police power as unreasonable to adduce facts which prove it to be so.

Referring to one of the evils which might be remedied, the opinion states:

> "* * * Moreover, lack of a uniform scale of commissions allowed local agents for the same service *may encourage unfair discrimination among policyholders by facilitating the forbidden practice of rebating.* In the field of life insurance, *such evils led long ago to legislative limitation of agents' commissions.*" (282 U. S. 257. Italics supplied.)

In the light of the foregoing principles the question is presented whether there exist, in the conduct of the Virginia insurance busines , evils for which our statute affords an appropriate remedy in whole or in part.

The Evils to be Remedied

The objects and purposes of the statutory provisions here challenged are to discourage, correct or remedy a number of evil and harmful practices now prevailing in the conduct of the insurance business relating to contracts made outside of Virginia but covering risks in Virginia. These practices sought to be corrected, in whole or in part, may be briefly summarized as follows:

(1) Rebating or rate-cutting by insurance companies to assureds.

(2) Rebating to assureds of part of their commissions by nonresident brokers.

(3) Unfair or unlawful competition between nonresident brokers and Virginia resident agents.

(4) Unfair or unlawful competition between foreign insurance company "groups" and Virginia insurance companies.

(5) The removing from Virginia of a large part of her insurance agency commission business and depriving the State, her insurance agents and citizens generally of the benefits incident thereto, and centralizing this business in New York.

(6) The lack of an impartial local agent to service Virginia risks contracted for outside of the State.

These practices will be discussed separately in the order named.

(1) *Rebating or rate cutting by insurance companies to assureds*

As has been shown heretofore the practice is prevalent among the insurance companies in dealing with New York City brokers to bid against one another on a program of proposed coverage for large national corporations, the program embracing not only numerous coverages of the same line in many states, but also combining coverages of all types of fire, casualty and surety risks in one proposal. It is customary to bid one price on the whole hotchpotch combination. As to some of the risks in some of the states, there are fixed rates, prescribed by law, which as to other risks there are no fixed rates in many of the states. The obvious effect of this practice is the inclusion in the bid price at a nominal figure, or at a ridiculously low figure, many risks as to which the rates are not prescribed by law, while listing at the proper rates those risks which are so prescribed. In a case of this kind, of course, no actual rate is adhered to, in fact, on any of the risks. It is a mere matter of juggling the figures on the non-fixed rates so as to arrive at the bid price for the whole. Virginia Code, section

4222(c) prohibits any insurance company from offering, paying or allowing any rebate of premium.

This practice of rebating, which in the opinion just quoted from this Court held to be an "evil," is comparable to that which formerly prevailed among brewers of giving or lending a retailer his fixtures, or selling him ice or other supplies, or renting him the premises at greatly reduced prices to induce him to handle the brewer's product exclusively. This insidious custom is now expressly prohibited by section 53 of the Virginia Alcoholic Beverage Control Act, and it is made a misdemeanor for any manufacturer, bottler or wholesaler of alcoholic beverages, "either directly or indirectly [to] sell, rent, lend, buy for or give" to any retail licensee "any money, equipment, furniture, fixtures or property with which the business of such retailer is or may be conducted." Section 41 of said act goes further and even prevents the sale of beer to retailers "except for cash."

If an insurance company should give an assured without charge a policy covering an open rate risk, provided such assured would contract for another risk at the rate prescribed by law, the obvious effect is a rebate and a violation of the legal rate as to the latter risk. And yet there is no difference, either in principle or result, between such a case and the practice followed by the appellant companies in bidding on these hotchpotch contracts.

The Court may properly inquire at this point: In what way does this statute tend to remedy this practice?

In the first place, the fact that the insurer is required to pay full commissions and hence not give the assureds the benefit of a reduction or rebate the brokers may make in their commissions tends to more nearly equalize the cost of insurance to the assureds, which is the primary objective in prohibiting rebates. Under present practices,

the chain stores buy their insurance cheaper than the local Virginia merchant (Op. R. 51-2).

In the second place, the fact that information respecting such a hotchpotch contract will become known to the independent resident commission agent when he countersigns will tend to discourage the practice.

Thirdly, the fact that such agent will acquire such information when countersigning the contract will enable the State, through reports, to secure it from such agent, and take such steps as are necessary to correct the evil. Unless the State is deprived of jurisdiction to prescribe Virginia coverage rates in contracts made outside the state, these hotchpotch contracts obviously violate Virginia rate-fixing laws [Virginia Code, sec. 4222(c)], and the resident agent, associated with a part of such a transaction, could be required to disclose such violations to the Bureau of Insurance.

(2) *Rebating to assureds part of their commission by nonresident brokers*

This customary practice which New York brokers follow and which is prohibited to resident agents [Code of Virginia, sec. 4222(c)] will be completely eliminated, because the insurance company is required to pay the full producers commission to the Virginia agent. While he may pay the New York broker half of the commission it is not likely that the broker will rebate any part of that.

(3) *Unfair or unlawful competition between the nonresident brokers and Virginia Resident Agents*

C. F. McNeil, one of the appellants, who is Richmond Branch Manager for the appellant Travellers Company, admitted that the New York brokers are given a better

rate by the insurance companies than these companies will give to a Virginia agent; whether the contract is one permitting equity rating or experience rating, and that a Virginia agent would have little chance in such a competition (R. 624-5). Mr. McNeil did not predicate his statement either on the practice of rebating by the New York broker, or on the practice of the companies in bidding on hotchpotch contracts. He had reference solely to contracts covering a specific risk which was subject to special rating. Of course, where, in addition to the lower rate, the bid price is also reduced by the amount the New York broker rebates from his commission, it is quite obvious that the Virginia resident agent has no chance in the world of successfully negotiating a contract in competition with the broker. If the *New York producing agents* have found it impossible to compete with the *brokers* who hawk and peddle the contract around, and as a result have been put out of business (R. 861), what possible chance can a Virginia resident agent have in such a contest?

This competitive advantage which insurance companies give New York brokers over Virginia agents is certainly an unfair one. The practices of giving these brokers better rates, of permitting rebating of their commissions, which the Virginia agent is forbidden by law to do, cannot be defended on any principle of fair play. Nor can there be any defense of the practice of permitting New York brokers to negotiate hotchpotch contracts including Virginia risks in which the rate is fixed by law. There can be no doubt that these bid prices on such contracts cannot lawfully be contracted for in Virginia. The inevitable result of these practices is a gradual flowing to these New York brokers (who are really auctioneers,

auctioning of risks located in other states) of the business of negotiating contracts for large risks. Even a large corporation domiciled in Virginia, and whose business is confined to Virginia, would have a strong incentive to combine all its risks in one "bid price" contract and therefore to send the business to these brokers to auction off among the insurance companies.

The effect of the statute here challenged is to adjust to some extent this competitive advantage enjoyed by the New York broker over the Virginia agent by requiring the association of the latter in all Virginia coverage business.

(4) *Unfair or unlawful competition between foreign insurance company "groups" and Virginia insurance companies.*

Virginia has no group of affiliated fire, casualty and surety insurance companies. The domestic fire insurance company must adhere to the standard rate filed with the Bureau of Insurance, while the domestic casualty company must conform to the rates fixed for workmen's compensation and automobile liability insurance. It is perfectly obvious that they have no shadow of a chance to compete with an affiliated group of foreign companies who bid on a hotchpotch contract combining not only all these lines but also including in one price risks in numerous other states as well as Virginia. Section 4222(c) of the Virginia Code prohibits an insurance company, not only from giving any rebate of premium to an assured, "as an inducement to any person to have issued any contract of insurance of surety," but also makes it unlawful for such company to offer "any inducement whatever, *not specified in the contract.*" This means specified in the

Virginia coverage contract itself, not a hotchpotch contract which includes as merely a part the underlying subordinate Virginia coverage contract (R. 125). In Virginia, automobile liability policies issued to public carriers are required to be filed with the State Corporation Commission, while workmen's compensation policies must be filed with the Industrial Commission. The practice is to file, not the entire hotchpotch contract, but only the underlying Virginia coverage contracts (R. 125). These contracts certainly would not show on their faces the fact that there was a hotchpotch contract, the price for which had been arrived at after competitive bidding and after giving the assured, as an inducement to make same, the benefit of reductions or rebates in the brokers' commissions. It is apparent that a Virginia insurance company cannot compete with such rebates and other unlawful "inducements."

As to the benefit which the Virginia insurance company would derive from this statute—it is not so clear and direct as that the agent will receive. The omission from the bid price of the brokers' rebate of commission would more nearly equalize the cost of the insurance. Also the enactment of similar statutes in other states will at least prevent the brokers from rebating part of their commissions on risks in other states and prevent this rebate from being reflected in the bid price for the insurance. The brokers testified that if this should happen they would have to go out of business. This would have the effect of removing the insurance business from the auction block and returning it to the agents where it properly belongs. It probably would also result in the elimination of hotchpotch interstate contracts. In any event, judicial confirmation of the state's jurisdiction to

exercise its police power in connection with these out of state transactions will make possible the passage of legislation which can correct the evil.

(5) *The removing from Virginia of a large part of her insurance agency commission business and depriving her insurance agents and citizens generally of the benefits incident thereto, and centralizing this business in New York.*

States compete for business to be carried on within their borders, just as nations compete in world commerce. States and municipalities have chambers of commerce whose principal functions are to bring business into their respective spheres of activitiy. Virginia's Conservation Commission has been given liberal appropriation by the General Assembly to advertise and attract business to the State. The happiness, prosperity and well being of her people are dependent upon the transaction within her borders of a satisfactory volume of business. To promote this prosperity is a proper and legitimate purpose for the exercise of the State's police power. (See cases cited, *supra.*)

Insurance against risks by industries engaged in business activities in the State is but a normal incident to that industry, and this insurance is naturally regarded as legitimate Virginia business; one which, in a broad sense, belongs to her citizens. The money to pay the cost of insurance covering Virginia activities is a charge against that activity and is earned through its operation. It is clear from the testimony of appellants' own witnesses in this case that Virginia has been deprived of the cream of this insurance agency business by unfair and destructive practices of rebates and rate cutting and by dis-

criminatory favors granted to the New York broker. The average assured in Virginia is also discriminated against by preferential rates given the national corporation.

The effect of this act will be to remedy to the extent of at least fifty per cent the discrimination against the agency business, and to a considerable extent that against the local assured.

Centralization of the conduct of the nation's business in New York, it is generally believed, is one of the chief causes of business and industrial dislocations. The present statute tends to bring Virginia business back to Virginia.

(6) *The lack of an impartial Virginia agent to service Virginia risks contracted for outside the state*

It is not necessary to repeat here what has already been said and what will hereafter be said with respect to the valuable services customarily rendered both to the insurer and the assured by the Virginia commission agent who alone is able to render such services. The testimony of the appellees' witnesses Tabb, DeJarnette, Clark and Boswell, all of whom are Virginia agents, covers the ground completely and in detail. What they have to say is corroborated by some of appellants' own witnesses and by public addresses of insurance executives hereinabove quoted from. Prior to this statute it was rarely the case that a Virginia resident agent was associated with the New York brokers in casualty and surety contracts, so that neither the insurer nor the assured has had the benefit of this service in these risks. Furthermore, the State has been deprived of the services of these Virginia agents in the prevention of accidents in these workmen's compensation and fleet au-

tomobile liability risks, which they customarily render in connection with contracts they negotiate or with which they are associated (R. 381-2).

The Virginia Association of Insurance Agents, (through whose members about 85% of Virginia insurance is negotiated), has indicated that as a result of this statute all these services will be hereafter rendered by those agents who countersign and receive the statutory compensation for being associated with the risks. (See resolution quoted *supra*.)

The existence of all these evils, however, will not justify the challenged legislation if it is arbitrary, capricious or unreasonable, which question will now be considered.

THE REMEDY PROVIDED BY THE STATUTE IS REASONABLE

That these practices of rebating of brokers' commissions and rebating of premiums and offering of unlawful inducements, in violation of Virginia laws, exist cannot be denied. In fact their existence is proven by the appellants' own evidence. That they are harmful to, and discriminatory against, the general run of Virginia assureds, all Virginia insurance companies and all Virginia commission agents is patent and obvious. Yet in the face of this deplorable condition which now exists, and for which the appellants are responsible, they come into this Court and set up the claim that *they* are being discriminated against by this statute. They evidently entertain the view that they have the constitutional right to engage in unlawful discriminatory practices, and that any law which corrects or tends to correct their discriminating against the people of Virginia is itself a discrimination against them. If Virginia is to permit any lawful discrimination at all under her statutes it is but natural

that it should be in favor of and not against her own citizens. But there is no discrimination. The evidence shows that every legitimate premium rate is loaded with a certain percentage for agents' commissions. The statute merely provides that this percentage which is allocated to this commission shall be paid to a Virginia commission agent, with the proviso that he may, in turn, pay not more than half of it to a Virginia licensed nonresident broker if he negotiates the contract and the Virginia agent is associated with him. As a means of assurance that the above requirement will be complied with, the insurance company licensee is prohibited from issuing any Virginia coverage contract unless such commission agent who is associated with the transaction countersigns same. These two requirements constitute the remedy provided by the statute for the evils pointed out above. It cannot injure the appellants for the Virginia agent to retain at least half of that part of the premium dedicated to the payment of the agent's commission. The suggestion is made in the record that, unless the practice of rebating by brokers is continued, the appellant companies will have difficulty in meeting the competition of mutuals. But the appellants have no vested constitutional right to resort to unlawful practices to meet lawful competition.

Furthermore, the uncontradicted testimony of many witnesses shows that for about fifty years it has been customary in the fire insurance line for most policies to be countersigned by a Virginia resident commission agent and for him to receive a commission of twenty per cent where he negotiates the contract; and in cases where the contract is negotiated by a broker outside the State, the Virginia countersigning resident agent associated therewith has customarily received 10%, or one-half of the

commissions. And not only is this true of Virginia, but the uncontradicted evidence is that a like custom prevails throughout the United States in the fire insurance business. This custom has not proven destructive to the fire companies affiliated with the appellant casualty and surety companies, and no reason has been pointed out why there should be any different result in its application to the casualty and surety business. It is difficult to conceive how a practice as arbitrary, capricious and unreasonable as the appellants claim this to be could have grown up naturally in the fire insurance business throughout the entire country. And yet the sole effect of the statute here challenged is to compel the casualty and surety companies to conform to the same practices which custom itself has established for the fire insurance companies. In fact the appellants' witness, Nicholls, New York Branch Manager of one of the appellant companies admitted the justice of participation in these out of state negotiated contracts by the resident commission agent, and the propriety of regulating same by law. He said, "I believe if the producers and the companies could get together on a uniform law affecting this thing, that much of this trouble that this is about to create could be eliminated, and it seems unfortunate that that has not been done before" (R. 159). Appellants' broker witness Otis testified that it is getting to be the custom generally in the United States for the local agent to expect participation in contracts covering risks in his territory (R. 882).

As to the basis of participation, the appellants claim that the requirement that the Virginia agent receive half of the producer's commission is unreasonable. However, the undisputed evidence shows that this is the practice the fire insurance companies and their agents have estab-

lished, and further shows that there is no reason for applying a different basis in the casualty and surety lines. The appellants' broker witness Gessner testified he could think of no reason for making any distinction (R. 928). On the other hand, appellees' witness Tabb testified that the resident agent would normally render more valuable local service in the casualty and surety lines, because of changing conditions, than in fire risks (R. 361). This statement was not in any way contradicted by any other witness. (See opinion below R. 61-2.)

In view of this old established custom in the fire insurance business of paying the resident agent half the producers' commission on contracts negotiated outside the state covering risks in his territory, and of the further undisputed fact that there is no reason for making any distinction in this respect between the fire line and the casualty and surety lines, it is difficult to understand upon what theory the claim is made that the statute which establishes the same practice in the casualty and surety lines is arbitrary, capricious and unreasonable. The practice in the fire business has grown up throughout the United States as the result of many years of experience, and has proven successful. It must be based on considerations of justice, equity and fair play. In fact, if the statute prescribed a different basis of participation for the casualty and surety business than this which has proven itself just throughout these years, it might indeed be challenged as unreasonable or arbitrary in disregarding these established standards of practice.

The appellants claim that the requirement that these out of state contracts covering Virginia risks *shall be countersigned by a resident Virginia commission agent* is unreasonable and arbitrary. On the contrary, it is

obvious that this is absolutely necessary to insure the company's compliance with the provision requiring the payment of his share of the commissions to the resident agent, without which the harmful practices heretofore detailed will undoubtedly continue unabated. In the absence of the countersignature requirement there is absolutely no means of any agent knowing that the contract has been made. Of course, it will be argued that the appellant companies would associate him anyway if the law requires it. But laws are not enacted on the theory that there will be voluntary compliance. For the law to accomplish its purpose, effective means must be provided to prevent violations. It is obvious that the *principal safeguard* against violations of the statutory provisions for the association of local agents in these transactions on a compensatory basis, and their consequent rendition of the contemplated services, *is the requirement that the contracts be countersigned by these agents.* The mere fact that the appellant companies do not like it, or may be to some extent inconvenienced by the requirement, does not affect the constitutionality of the statute. Nearly all regulatory statutes cause inconvenience. But, with the exception of certain blanket policies, it has been a general voluntary custom in the fire insurance business for half a century, and if it had occasioned much inconvenience some other substituted method would undoubtedly have been devised.

The appellants seem to be proceeding in this case on the idea that this countersignature requirement is a very unusual sort of statute. But this is not true. On the contrary, statutes requiring countersignatures on these contracts negotiated outside the state by agents resident in the state of coverage have been in force for many

years in nearly all the states (R. 62). The fact that so many states have found it necessary to enact legislation similar to that here challenged speaks eloquently for the need of this type of legislation to correct the injurious practices heretofore pointed out which seem to be repugnant to their ideas, as well as those of Virginia.

In 1912 the General Assembly of Virginia enacted a statute prohibiting foreign insurance companies qualified in this State from making Virginia coverage contracts "save through regularly constituted agents of such companies residing in Virginia" (Acts 1912, 549-550). This was incorporated in the 1919 Code as section 4222. It was always interpreted as requiring the signature or countersignature of a Virginia agent upon all such contracts. In 1936 the statute was amended so as to include an express provision that such contracts should not be issued unless countersigned by such a Virginia resident agent. But the only effect this amendment had on casualty and surety contracts was to cause the insurance companies to have them signed by their own employees who were paid a salary. As the testimony heretofore pointed out shows, these employees considered their act of countersigning a mere perfunctory act which they would perform without even examining the contract. Then in 1938 the statute was further amended and a new code section 4221-a was enacted, the effect being to prohibit insurance companies from issuing such contracts unless countersigned by a regularly constituted Virginia resident *commission* agent. Section 4226-a was also amended to provide that this resident commission shall receive full commissions, with the proviso that he may pay to a Virginia licensed nonresident broker associating him with the contract not in excess of fifty per cent thereof.

It thus appears that the legislation here challenged is not entirely new but has been brought about by amendments to statutes already existing, the necessity for which amendments has been occasioned by the harmful and injurious practices of the appellant companies heretofore pointed out.

Appellants also contend that the practices complained of take place outside of Virginia and that it is unreasonable for the State to undertake to regulate the consequences of acts which occur outside its borders. But, as has been shown, the company's acts in carrying on these injurious practices are done *in the exercise of its Virginia license privilege,* and therefore are within the State's regulatory jurisdiction. Furthermore, while the acts *are done* principally in New York, *the harmful effects or results* of these acts *occur in Virginia.* It was very clearly decided in the Louisiana chain store case, (*Great A. & P. Tea Co.* v. *Grosjean, supra*), that a state may regulate a foreign corporation which has submitted itself to its jurisdiction by securing a license to do business therein, "to adjust competitive or economic inequalities," and that such regulatory action is a proper and reasonable exercise of the police power "irrespective of whether the evils requiring regulation arise solely from operations in Louisiana or are in part the result of extra-state operations." It is clear that it is not unreasonable for Virginia to undertake to correct the evil practice of these licensee appellants in granting rebates in connection with contracts negotiated in New York; and that to this end the State may properly exercise in Virginia its governmental control over them to which they submitted themselves when securing licenses to do business in the State. It is significant, in this connection,

to call attention to the fact that one of the evils stressed by the court in the chain store case was that the A. & P. Company "received in the year 1934, from its vendors, secret rebates, allowances and brokerage fees amounting to $8,105,000 which were demanded by the company as a condition of purchasing from the vendors in question." Most of these rebates were obviously received outside of Louisiana, but the effect thereof was felt by its competitors in that state. The testimony of appellants' witness, Thomas, is to the effect that these chain stores, through hotchpotch contracts, purchase their insurance cheaper than their independent competitors. This advantage enjoyed by these chains in connection with their insurance costs, and also enjoyed by other large corporations, operates to the detriment of their competitors in Virginia as well as Louisiana, and this statute will measurably adjust the discrimination in this particular item of the cost of doing business.

Appellants also contend that this statute is arbitrary and capricious because it interferes with the freedom of contract. But this Court has already held in *O'Gorman & Young* v. *Hartford F. Ins. Co., supra,* that the regulation of the commissions to be paid agents of insurance companies does not infringe that liberty. In the recent case of *West Coast Hotel Company* v. *Parrish,* 300 U. S. at p. 391; 81 L. ed. at p. 708, in sustaining the power of the State of Washington to prescribe minimum wages for women and minors in industry, Mr. Chief Justice Hughes said:

> "* * * In each case the violation alleged by those attacking minimum wage regulation for women is deprivation of freedom of contract. What is this freedom? The Constitution does not speak of free-

dom of contract. It speaks of liberty and prohibits the deprivation of liberty without due process of law. In prohibiting that deprivation the Constitution does not recognize an absolute and uncontrollable liberty. Liberty in each of its phases has its history and connotation. But the liberty safeguarded is liberty in a social organization which requires the protection of the law against the evils which menace the health, safety, morals and welfare of the people. Liberty under the Constitution is thus necessarily subject to the restraints of due process, and regulation which is reasonable in relation to its subject and is adopted in the interests of the community is due process." (81 L. ed. 708.)

The appellants further contend that the agents will do nothing to earn their part of the commission. But there is nothing except speculation and opinions of appellants' employees and New York brokers to substantiate this claim. The Virginia Association of Insurance Agents has taken the position that it is the duty of the resident Virginia agent who is associated with the nonresident broker to examine into the risk and satisfy himself as to the correctness of the rate and coverage embodied in the contract, before countersigning same; and that it is further his duty to render the same service in connection with the contract throughout its life as he would render if he alone negotiated it. Appellees' witness, Moore, enforcement officer of the Bureau of Insurance, testified that this Bureau expected similar services to be rendered the resident agent associated in these out of state contracts. Attention has already been directed heretofore to certain testimony of appellants' witnesses admitting the extent and value of the services customarily rendered by the resident agent in connection with casualty and surety

contracts, and to public addresses of insurance executives. The testimony of appellees' witnesses, four Virginia insurance agents, relating to the nature and extent of the services customarily rendered by them will now be considered in some detail.

The witness DeJarnette testified that in an automobile liability risk it is the custom of the resident agent to first study the classification and correctness of the rate applicable (R. 269). During the life of the policy the agent inspects the equipment, and also studies the conduct of the drivers in operating same, with a view to making suggestions to avoid accidents (R. 270). If it is a fleet automobile risk, certain credits apply to the rate applicable to cars more than five and, if there are more than ten cars, the assured is entitled to an experience rating after the fleet has been operated over a period of two years. This experience rating is promulgated by the Virginia automobile rating bureaus. The agent investigates the history of the risk and checks his information with the rates so promulgated (R. 270). During the life of the risk, the agent keeps a complete list of all claims reported and studies the accident frequency, with a view of advising the assured and suggesting preventive remedies (R. 270). When a loss is declared, the agent follows each stage of the adjustment closely, and, in most cases, makes out the report of the accident and turns it over to the claim adjuster and then follows it to its conclusion (R. 270). It is generally customary for the assured in case of a loss to contact the resident agent rather than the claim department of the insurance company (R. 271). The attitude of the agent with reference to controversies and disputes between insurer and insured, and in dealing with company

representatives, is to see that the policyholder obtains every right and benefit that the contract entitles him to, the agent considering it his duty to see that both the assured and the company are fairly treated—he regarding himself as an impartial representative of both parties (R. 271). The only compensation the agent receives for the services he renders during the life of a policy is the commission paid at the time the contract or policy is issued (R. 272).

In connection with a contract for workmen's compensation insurance, this witness testified that, before the contract is written, it is necessary for the agent to make a personal inspection of the plant, and also the payroll, so that the rate may be properly classified as to the various employees, the compensation risk being composed of different rates, depending upon the type of the work each employee is engaged in performing. When the agent has satisfied himself of these points, he then countersigns and delivers the contract (R. 272). He then advises the assured with reference to inspections by the insurance company's engineering department to determine if any additional safety appliances should be installed to prevent accidents, and when the engineering department reports the results of the inspection a copy is sent to the agent's office. Upon receiving the recommendations of the engineering department, the agent then discusses with the assured the question of whether or not the recommendations justify the necessary expenditure to carry them out. In some cases the agent works out with the engineering department improvements of their recommendations (R. 273). When an accident happens, the policyholder usually reports the matter to the agent, who in turn reports it to the company (R. 273). Whenever the agent feels that the assured should

have any service rendered by the engineering or inspection division, he calls the service department of the insurance company and requests same (R. 273-4).

This witness' company is not a party to this suit and the witness has customarily been associated with the non-resident broker in contracts negotiated outside the State, receiving half the commissions. In these cases it has been customary for him to examine and check every such contract and see that all the rates and forms are properly applicable to Virginia requirements, and, if not, to correct the same. He retains a copy of the contract for his files. He has been called on for service by the assured in such contracts in which he has been so associated (R. 274-5). During the life of the contract, the agent makes a continual study of the risk and suggests any change as to rates, forms, or privileges to which the assured is entitled but which may not have been applicable at the time the contract was issued, and he secures an endorsement from the insurer to conform to the changed conditions (R. 275). This witness stated that, in his opinion, the resident commission agents of Virginia throughout the state will, in conducting their business, perform the duties as set out in the resolution of the directors of the Virginia Association of Insurance Agents heretofore quoted (R. 278).

The witness Robert R. Boswell is a resident commission agent and has had extensive experience in the casualty and surety business. He testified that when a contract of insurance is on the books of a resident agency the service of the agency has only just begun, and that it is up to the agent to maintain a sufficient force to service whatever may happen under the contract during its life (R. 302).

In connection with contractors' bonds, the agent makes periodic visits to his assured to improve the loss ratio and points out any unusual hazards around their plants. He suggests safety ideas to the assured to reduce accidents. He sees to it that the safety engineer of the insurance company is on the job at the inception of the risk and keeps in close contact with the safety engineers to secure periodic visits and reports (R. 302-3). Prior to the writing of the contractor's bond, the agent satisfies himself that the contractor has not obligated himself to do more than he is financially able to do, that he is familiar with the type of work involved, and that he has the proper kind of equipment. He advises with him as to the employment of sub-contractors, and keeps well posted and informed as to who these sub-contractors are so that the most satisfactory sub-contractor will be available for the particular work at hand (R. 303-4). Where a foreign contractor has a public contract, such as a road construction job, the agent keeps in contact with the State Departments to the end that payments will be promptly made on the contract (R. 304-5).

The witness Roger E. Clarke is a resident insurance agent at Fredericksburg, Virginia, and in the past was the president, and a member of the board of directors and various standing committees of the Virginia Association of Insurance Agents. He testified that ever since he has been in the business it has been customary to divide equally the commissions on fire insurance business originating outside of the State (R. 328). As to the service it has been customary to render in connection with such fire policies, he testified that, when the agent is associated with the risk directly by the company, he conducts his investigation of same just as if he were the producing

agent. He makes an examination to determine the desirability of the risk and reports his recommendations with respect thereto. The agent then prepares the policy in accordance with the facts disclosed by his investigation, applies the proper rate, countersigns same, and transmits it to the company. Thereafter he holds himself in readiness to service the risk during the life of the policy. The assured is informed that the agent is associated with the nonresident producer to render such service as is appropriate, and that there is no increase in cost of the insurance to the owner of the property by reason thereof. He regards himself as an impartial representative of both the insurer and the assured (R. 329-330). His testimony with reference to the service customarily rendered by the agent in connection with workmen's compensation risks and automobile liability risks (R. 330-331) is substantially the same as that given by the witness DeJarnette heretofore referred to. He stated that the agent also makes investigation of the premises covered by a public liability policy and works in cooperation with the insurer's engineering department to eliminate hazards. The witness testified that the services he described as being customarily rendered in these three types of risks is somewhat typical of an agent's services in connection with the other various types of coverage involved in casualty insurance (R. 331). The agent consults with the Virginia Auto Administrative Bureau and the Virginia Insurance Rating Bureau with reference to the rates applicable to risks with which he is connected (R. 332). When loss occurs the agent follows the negotiations and settlements of claims from the inception to the conclusion, assists in the preparation of proofs of claim, advises the assured as to acts on his

part which might prejudice his rights, and generally sees that a settlement fair to all parties is arrived at (R. 332). The commission agent customarily regards it as his duty to protect the interests of the assured, whom he considers his client, and he is generally available to the assured for consultation and advice with respect to the interpretation of contracts, the assured's duties thereunder, or any other matters relating to the coverage (R. 333).

He further testified that it is his intention to comply with the provisions of the resolution of the insurance agents association outlining the duties of resident agents, and that it is his belief that the agents throughout the State will do likewise (R. 334).

This witness further stated that, in his opinion, a nonresident broker or agent is not in a position to render as satisfactory service to the assured or to the insurer in connection with local Virginia risks as the resident agent, unless said nonresident agent personally visits the State and familiarizes himself with the conditions pertaining to the risk, giving in detail his reasons therefor (R. 334).

The witness T. Garnett Tabb is one of the most successful and prominent commission insurance agents in Virginia and has been connected with the business for about forty-seven years. He testified that it is generally understood that a commission insurance agent recognizes his first duty to his policyholders as a matter of good policy, though he would not forget his allegiance to his company's interests. In cases of conflict between the interest of the two, the agent acts as arbitrator and frequently gets both parties together, preventing court action, and finally satisfying both parties as to the justice of the conclusion reached (R. 355). For at least twenty-five years it has been customary for the Virginia

resident commission agent to receive one-half of the producer's commissions on Virginia fire risk contracts originating outside of the State (R. 384). When such contracts are sent to the agent, he studies its provisions and determines whether the correct rate has been applied. He feels responsible for the correctness of any contract he countersigns. The agent sometimes inspects the risks in these fire insurance cases sent to him, if he entertains any doubt as to the correctness of the coverage or rates, and makes any suggestions which his inspection renders appropriate. As soon as the contract is in such form as to meet with his approval, the agent then countersigns it and either returns it to his home office or sends it direct to the broker from whom he received it, if it was sent by a broker (R. 357). During the life of such a policy, the agent would expect to respond to any request for service from the assured or its representatives, if a foreign corporation, and "he would expect to render to both his company and the insured just the same service, if it was needed" as he would render if a Virginia agent had negotiated the contract (R. 357). He testified that it has usually been the practice in such cases for the agent to write either the broker or the assured at the time he countersigns the policy, offering his services (R. 357).

In connection with casualty and surety risks, the witness testified that the first duty of the agent is to see that the policy is correctly written, and thereafter it is his duty to keep in close touch with the assured and look forward to rendering "super-service" to enable him to hold the business, and perhaps increase his business with that assured (R. 357-8).

In connection with fleet automobile liability risks, the agent sees that the rates applicable to the various terri-

tories where the cars are domiciled are correct and properly classified; he makes a more or less continuous study of the risk and its loss experience, and frequently has the investigation and claim departments of his insurance company call the drivers into consultation for safety measures. The agent himself often participates in these safety meetings (R. 358-9). He stated further that, in his opinion, actual contact by the agent with the physical conditions pertaining to a casualty risk is necessary to properly service same, and that the nonresident broker or agent living in New York or Chicago cannot possibly render as satisfactory service to the assured as the local Virginia agent (R. 359); that a personal contact with the operation of the industrial activity of an assured in order to properly perform a commission agent's service is most imperative (R. 359). The witness testified that he knew of no valid or substantial reason why a distinction should be made in the basis of the division of commissions between a nonresident agent or broker and a local resident commission agent in the casualty and surety lines and fire insurance line where a Virginia risk of either type is negotiated through a nonresident agent or broker (R. 361). The Travelers Insurance Company which he represents advertises nationally that it has thousands of agents ready to take over the responsibilities of the assureds promptly, no matter when or where an accident happens, and the local commission agents cheerfully render this service (R. 362). Prior to the 1938 Act, there was no established practice in Virginia with reference to the basis of division of commissions in cases where a Virginia resident agent was associated with a nonresident agent or broker in casualty and surety contracts, or in any line except the fire insurance line (R. 363).

This witness testified further that the resolution hereinbefore quoted, which was adopted by the directors of the Virginia Association of Insurance Agents, is in conformity with the practice which has heretofore prevailed in Virginia in connection with the fire insurance business, where the Virginia coverage contract has been negotiated by a nonresident broker and the contract has been forwarded to the agent by the insurance company, with the exception that in the past it has not been customary to contact the assured (R. 364-5). In the witness' opinion the outline of duties contained in the resolution to the effect that the agent should contact the assured in such cases "is simply a forward step in rendering more efficient service and making it a uniform practice" (R. 364-5). He stated in his opinion that an agent receiving one-half of the commissions "would consider himself morally obligated to render every possible service both to the assured, the broker and the company" and that the prospect of securing a renewal of the insurance would be an incentive to the performance of such service, as the Virginia commission agent and the nonresident broker will be jointly interested in servicing and retaining the business (R. 365). The witness stated that in his opinion 90% of the insurance business of the state written in Virginia is written by the members of the Virginia Association of Insurance Agents and its members will comply with the resolution (R. 365). This witness also stated the service customarily rendered in connection with interpretations of the contract for the assured and advice to him with respect to changes in conditions pertaining to risks are constantly occurring. It is customary for the agent to contact the rating authorities and confer with them regarding rate classifications, experience rat-

ings and other matters which enter into the premium cost. With reference to adjustments of claims, the witness contrasted the difference in viewpoint entertained by a company employee, such as a claim adjuster or a branch manager and that of a commission agent. With respect to countersigning a policy, the witness pointed out that whereas the countersignature by the company representative is generally regarded as a mere perfunctory act because it is, in effect, only "one more signature of the company assuring the policy," on the other hand, it is to the interest of the commission agent for his own profit in the future to be very particular about applying his signature to a contract without knowing it to be correct. For this reason, the commission agent feels that he is taking a responsibility when he affixes his signature thereto. This same incentive impels the agent to carefully service the contract during its life (R. 365-7).

This witness further stated that the records in the office of an insurance agent, with respect to insurance contracts countersigned, provide information from which the insurance department may accurately determine the volume of insurance written out of the State by the insurance companies, for use in ascertaining the correct amount of taxes properly payable thereon (R. 366-7). This, of course, is a service the agent may render directly to the State.

The testimony of these witnesses, which has been referred to and much of their testimony which it would unduly prolong this brief to review in greater detail, establishes beyond any doubt that the Virginia commission agent renders many valuable services which, in the nature of things, a nonresident broker cannot render, because he has no personal knowledge of the circum-

stances and conditions pertaining to the risk. There is no real dispute that Virginia agents do perform these services, but the appellants claim that the insurer's engineering and claims departments do similar work and this enables the New York broker to dispense with the services of the impartial agent at the locality of the risk. But the services of an employee of the insurer are of an essentially different character. The employee's actions are naturally influenced and dictated by his employer's interests. He views every act and recommendation from that standpoint, and not primarily to promote the interests of the assured. On the other hand, the commission agent, being dependent upon the goodwill of the assured for the retention of the business on his books, is motivated by this incentive to look out for the assured's interests. If the assured feels that his interests are not properly taken care of, he will place his business with another agent. He looks to the agent for satisfactory service and protection, not to the insurer, and the agent knows this. He, therefore, as a matter of self-protection, bends every effort to see that his client receives fair treatment from the insurer. He is on the ground, in close contact with developments, where he can see that this is done. He controls the placing of the business and if the insurer acts unfairly may transfer it to another company. The company knows this and is as anxious to please the agent as the agent is to please the assured. For this reason, any reasonable request which the agent makes of the company will be complied with.

And the companies themselves invariably emphasize the value of the local commission agent's services to the assured, and stress its importance as an argument to offset the cheaper cost of mutual policies. An illustration

of this is found in a quotation from a public address delivered by Mr. Lawrence E. Falls, Vice President of the American Insurance Company of Newark at a meeting of the New Jersey Association of Underwriters on March 9, 1939. This Insurance Company is under the same management and control as the Bankers Indemnity Insurance Company, one of the appellants in this suit. In the course of this address Mr. Falls said:

> "There are insurance companies which sell their policies directly to the insured, and employ no agents. Most such companies hold out to the insured that their plan of operation saves the insured the amount of the agent's commission, and, therefore, those companies advertise that they can sell as good indemnity at a premium cost less than that charged by companies represented by local agents. Of course they do not mention that *the assured will be deprived of the services of a local agent when the contract is prepared;* through the currency of the policy *as changes in the assured's business require changes in the* policy; and at the *time of a loss,* when the *home office of the insurance carrier* and the *location of the insured's business* may be *hundreds, or thousands, of miles apart.* Insureds who buy contracts of indemnity in companies *represented by local agents to whom a commission is paid,* are, in increasing numbers, becoming aware (and most of the large insured are already aware) that *the insured, and not the insurance company, pays the agency commission.* In view of these two truths alone (and I hold that they are truths), the right rate of commission, one which will permit our present system of insurance distribution to continue, and to be patronized by the preponderent majority of insurance buyers in this country must be that proportion of the premium which the agent convinces the assured that he, *the agent, earns by his*

service to the assured and to the insurance business.

"I know of one specific instance where the agent talked this matter over with the assured in plain English and with simple arithmetic. The premium was $6000. a year, and the agent's commission was 20 per cent, of which fact he informed the assured, and stated that he, the agent, was on the assured's payroll for $1200. a year—or $100. a month. When he first wrote the account, the premium for this same amount of indemnity was $8500. a year. Through periodic inspections of the plant, removal of unnecessary hazards and, therefore, improvement of the risk, the rate had been reduced to save the assured $2500. a year. *The agent reformed the policies* so often as the nature of the assured's business required their reformation, and the agent asked the assured point blank whether or not he was worth $100. a month to the assured as an employee. The assured said, 'Yes,' and *that account is not subject to attack by direct-writing companies, nor by mutual and reciprocal carriers, even though they pay alluring dividends.*"

What a remarkable difference there is in the opinions of the value of the local commission agent expressed by these insurance executives in public address to their associates and the attitude toward these agents taken by the appellants in this case. In public addresses they say *salaried employees of mutual companies* cannot possibly render services at all comparable to the *local commission agent*, while, in this record, they claim that *salaried employees of stock companies* do and can render this service to the assured as well or better than the *local agent*.

The appellants contend that residence of a commission agent in the state is an arbitrary and capricious thing upon which to predicate a statutory regulation. But the Supreme Court itself has approved regulations based

on such residence in the case of *La Tourette* v. *McMaster, supra,* in which was challenged the validity of a statute of South Carolina prohibiting the granting of an insurance broker's license to any person unless he was a resident of the state and had been a licensed insurance agent of the state two years. La Tourette was not a resident of the state, but a New York broker who evidently desired to solicit in the state the privilege of peddling South Carolina risks among New York insurers. He claimed he was being deprived of his rights as a citizen of the United States in violation of the Fourteenth Amendment. In reply to this Mr. Justice McKenna said:

> "This contention depends upon the character of the business of insurance, and it was decided in *German Alliance Ins. Co.* v. *Lewis,* 233 U. S. 389, 58 L. ed. 1011, L. R. A. 1915C, 1189, 34 Sup. Ct. Rep. 612, to be clothed with a public interest, and subject, therefore, to the regulating power of the state. And it necessarily follows that, as insurance is affected with a public interest, those engaged in it or who bring about its consummation are affected with the same interest and subject to regulation as it is. A broker is so engaged,—is an instrument of such consummation. The statute makes him the representative of the insured. He is also the representative of the insurer (*Hooper* v. *California,* 155 U. S. 648, 657, 39 L. ed. 297, 301, 5 Inters. Com. Rep. 610, 15 Sup. Ct. Rep. 207), and his fidelity to both may be the concern of the state to secure. As said by the supreme court of the state: 'It is important for the protection of the interests of the people of the state that the business should be in the hands of competent and trustworthy persons.' (104 S. C. 504, 89 S. E. 398.) *And we may say that this result can be more confidently and completely secured through resident brokers, they being immediately*

under the inspection of the commissioner of insurance. The motive of the statute, therefore, is benefit to insurer and insured, and the means it provides seems to be appropriate.

" 'But we need not cast about for reasons for the legislative judgment. We are not required to be sure of the precise reasons for its exercise or convinced of the wisdom of its existence.' It is enough if the legislation be passed in the exercise of a power of government and has relation to that power. *Rast* v. *Van Deman & L. Co.*, 240 U. S. 342, 365, 366, and cases cited; also *Bunting* v. *Oregon*, 243 U. S. 426, 437." (248 U. S. 467 8. Italics supplied.)

The South Carolina statute in the above case goes much further to retain state control of its insurance broker's business by confining its conduct solely to residents of the state than the statute here attacked.

But the last paragraph quoted above serves as a forcible reminder of the erroneous approach which the appellants have adopted to determine whether the Virginia statute is arbitrary and capricious or whether it is a reasonable exercise of the police power. Their attitude seems to be that the burden is on the State to prove facts which would sustain a recovery in an action on a *quantum meruit* by a resident agent for half the commissions on an insurance contract negotiated in New York, and they further seem to contend that the value of the agents' services on such *quantum meruit* should be restricted to a consideration of his acts in affixing a perfunctory countersignature to the contract and nothing more. They assert that since the statute does not require the resident agent to do anything except countersign that the court must conclusively assume that this is all that it was contemplated by the statute that he would do. But this

is an obvious *non sequitur*. Neither the General Assembly nor the State Corporation Commission, in fixing the percentage of the premium which is allocated to agents' commissions, has undertaken to prescribe the measure of the services the agent shall render in return therefor in connection with business he alone produces. Custom and the self-interest of the agent to retain his client's business may be relied on to take care of the amount of service he will render. It must be presumed that the legislature knew the customary functions of the impartial commission agent as well as the nature and extent of the services such an agent ordinarily renders, and contemplated that the resident agent associated with such a contract will render these customary services and that they would be commensurate with the compensation provided therefor. Certainly this Court will not assume that the General Assembly created what one of the New York broker witnesses termed a "gravy train" for the Virginia agent and upon this unwarranted assumption, declare the act unconstitutional. On the contrary, the rule is well settled that the Court will adopt that construction which will sustain the statute, not destroy it, and will not impute an intention to the legislative body to enact ridiculous legislation. *Stephenson* v. *Binford*, 287 U. S. 251, 277.

Appellants also contend, because the national corporations are at liberty to request the association with the New York broker of a Virginia resident agent if they so desire, that the fact they do not more frequently request such association in casualty and surety cases shows that the local agent's service is without value to them. But this argument leaves out of consideration that the association of the resident agent is inconsistent

with the practice of auctioning off the hotchpotch contract. In the price bid for such a contract is reflected the rebate which the broker yields out of his customary commission. The association of the resident agent requires payment to him for his services and this payment interferes with the broker's rebate of commissions, because he cannot rebate that which must be paid to the local agent. The effect of this is to increase the bid price and reduce the advantage in insurance costs which the national corporation enjoys over its independent Virginia competitor.

And right here lies one of the principal causes of opposition to this statute. It is no secret that the same banking and financial interests which control some of the national corporations also control some of these large insurance groups. The national corporations have thrived on secret rebates and other competitive advantages they have enjoyed over smaller locally owned competitors. Naturally they and their business allies resist to the uttermost any move which reduces this advantage or tends to adjust these competitive inequalities. Nor is the existence of this rebating evil, or efforts to overcome it, anything new. It formerly existed in connection with railroad and other public utility rebates until remedied by both state and federal legislation carrying severe penalties and punishment for such favoritisms. It was practiced in insurance contracts in Virginia until 1912, when it was found necessary to prohibit it and to prescribe heavy penalties for those engaging in the practice (Acts 1912, p. 547). These provisions of the Virginia statute are now being evaded and circumvented by the practice of making the contract outside the State and defying Virginia's jurisdiction and power to do anything about it.

It is inconceivable that the Constitution of the United States can be so construed as to deny to the State the power to prevent its licensees from exercising their license privileges in such a manner as to so flagrantly flout the State's laws.

The statute here attacked will effectually prevent rebating by nonresident brokers, as hereinbefore pointed out, and will measurably adjust the competitive inequalities between the Virginia agent and the nonresident broker as well as between the locally owned business and the national corporation.

Unless this State may by legislation regulate the making by its licensees of Virginia coverage insurance contracts outside the State, there is only one recourse for the State to take to prevent rebating and to protect its citizens against this unfair competition. She may confine the conduct of these lines of the Virginia insurance business to corporations. (See the quotation from *National Union F. Ins. Co.* v. *Wanberg, supra.*) In addition she may refuse to permit these foreign casualty and surety corporations from engaging in the insurance business in the State. Thus, in the recent case of *Atlantic Refining Company* v. *Virginia*, 302 U. S. 22, 26, which involved the validity of Virginia's entrance fee imposed on foreign corporations for the privilege of doing business in the State, the Supreme Court said:

> "* * * Whether the privilege shall be granted to a foreign corporation is a matter of state policy. Virginia might refuse to grant the privilege for any business, or might grant the privilege for some kinds of business and deny it to others. It might grant the privilege to all corporations with small capital while denying the privilege to those whose capital or resources are large. * * *" (302 U. S. 26).

The above case cites, with approval, the former decision of that court sustaining the validity of section 163 of the Virginia Constitution prohibiting foreign public service corporations from doing any intrastate business in Virginia; *Railway Express Agency* v. *Virginia*, 282 U. S. 440, 75 L. ed. 450.

And finally the state may, in order to insure regulatory control over her domestic insurance business, limit the *charter powers* of such domestic insurance companies so that the corporations will not have power to do business or *make insurance contracts outside the state. Ex parte Schollenberger*, 96 U. S. 369.

Therefore, what it is clearly within the power of the State to accomplish legitimately in this manner cannot be said to be arbitrary and capricious because the power is exercised in a different manner. In fact, it is a much more reasonable attitude for the State to permit foreign insurance companies to do business in the State upon condition that they will not make Virginia insurance contracts *anywhere* in violation of Virginia laws, than to exclude them altogether, and confine the business to domestic corporations.

Finally, in concluding the discussion with respect to appellants' contention that *the statute is arbitrary and capricious*, it is not inappropriate to repeat what has been heretofore quoted from *La Tourette* v. *McMaster, supra.*

> "'But we need not cast about for reasons for the legislative judgment. We are not required to be sure of the precise reasons for its exercise or convinced of the wisdom of its exercise.' It is enough if the legislation be passed in the exercise of a power of government and has relation to that power."

Furthermore, the court emphasized in the above case, in determining whether a statute violates rights under the fourteenth amendment, the difference between those statutes relating to ordinary occupations and those which are an exercise of the police power and undertake to regulate a business clothed with a public interest. The court said, with reference to the alleged violation of La Tourette's rights: "This contention depends upon the character of the business of insurance, and it was decided in *German Alliance Ins. Co.* v. *Lewis* * * * to be clothed with a public interest, and subject, therefore, to the regulating power of the state."

La Tourette had contended that the South Carolina statute, confining insurance brokers to residents of the state, had been passed solely in the interests of the local agents and brokers, and was therefore arbitrary. The court unanimously rejected that contention just as the similar contention of the appellants here should be rejected.

VI.

The Branch Manager Appellants Have no Standing in Court to Complain of the Statutory Regulation Requiring Insurance Companies to Make Insurance Contracts Through Regularly Constituted Virginia Resident Agents, Have Them Countersign the Policies, and Pay Them the Usual Producers Commission.

The challenged statute does not interfere with the performance by the branch manager appellants of any of the real duties pertaining to their office. It does not prevent them from signing contracts of insurance. It does not affect their compensation because under the well established practice in the insurance agency business they have never received, and are not permitted to re-

ceive, commissions. This was admitted by the Branch Manager Adair who said in the rare cases where he negotiates contracts he invariably turns the commission and the business over to one of the resident agents (R. pp. 234-5). The only change in his status is that the statute now requires the resident commission agent to countersign the policies, whereas he formerly did this. This same witness admitted that the countersigning was treated by the branch managers as a farce, that they never even examined the policy, unless through curiosity to learn of new practices, and that the countersigning was a "perfunctory matter." They did not even keep a record of the contract in their offices (R. pp. 209, 238-9, 252-3). These branch managers, therefore, having treated the statutory requirement and duty of countersigning as a joke, and having completely ignored the purposes for which it was imposed by law, now complain that the duty and responsibility have been transferred to resident agents who regard it as a serious obligation (R. 375-6). The branch manager received no additional compensation for countersigning, nor was any credit for the business given to his office. This went to the branch manager of the state where the business originated. The appellant Adair admitted that the only effect the challenged statute has on his duties and services, and the value thereof to his employer, is that it requires a commission agent to countersign the contract, and his signature is not sufficient to make the contract legally effective. He complains that his services are rendered less valuable because now the company has to pay someone else for the countersignature which he provided. But it is not the purpose of the statute to make the company pay merely for a countersignature. The purpose is to as-

sociate a commission resident agent with these transactions and to require a division with him of that part of the premium dedicated to the payment for the various services of a commission agent. The requirement that the commission agent countersign every such contract *is to insure that such an agent will be associated with the contract on a compensatory basis.* If he countersigns, he can then easily collect his compensation. The statute complained of is solely a regulation of the insurance companies prescribing the methods by which they shall transact business with commission agents and brokers, and how they shall be compensated for their services.

The branch manager, therefore, has no standing in court to complain of this regulation of the insurance companies they are employed by. It is not their compensation or duties which are affected but merely the division between agent and broker of the "producer's commission," none of which has ever gone to the Branch manager. A perfunctory countersigning is not a service, and never was a service when rendered by the branch manager.

These branch manager appellants are claiming that they have a constitutional right to perform this perfunctory act and thereby deprive the State of an effective means of enforcing compliance by the insurance companies with the requirements of the statute by having the countersigning done by the resident agent who is to be associated with the transaction and is to be compensated for his services therein. The mere statement of the proposition carries its own refutation.

It is clear, therefore, that the provision requiring the licensee insurance company to procure the countersignature of the commission agent to be associated with the

servicing of the contract is a regulation of the manner in which the insurance company must transact business under its license privilege, and is not a regulation of insurance agents. The branch managers cannot be heard to complain of the regulation of their employers.

VII.

The Statutory Classification of Agents and Employees of Stock Insurance Companies in Virginia is Not Arbitrary or Capricious, But is a Reasonable One.

The statute classifies commission agents, solicitors and nonresident brokers in an entirely separate class from salaried employees of insurance companies. The distinction between their customary and normal functions is obvious, as has been hereinbefore pointed out. The only effect this classification has upon the branch manager appellants in this case is to require their employers, the insurance companies, to have their Virginia coverage contracts signed by the impartial commission resident agent instead of by the company's employee who owes no obligation to anyone save his employer. One purpose of this, as has been shown, is to put it in the power of the resident agent to see that the provision of the act requiring him to be associated with the contract on a compensatory basis, *i.e.*, the payment of his commission, is complied with. But in addition thereto, there is another excellent reason why the requirement is correct and proper. Section 4222(c) of the Virginia Code prohibits both the agent and the insurance company from granting any rebate of premium to an assured, or any inducement not specified in the policy. The evidence is undisputed that the branch managers did not even examine the contract before countersigning to ascertain whether the rate was less than that fixed by law. Thus,

there might be an obvious rebate on the face of the policy. It is the duty of the agent to verify the correctness of the rate because if he countersigns a contract which carries a rebate he is himself punishable therefor under section 4223. The agent, therefore, owes the duty *to the state* to see that the rate is not *too low* while he owes *the assured* the duty to see that it is not *too high*. If he fails in his duty to the state, he is punishable by a fine of not less than $100.00, and this makes it very unlikely that he will treat it as a perfunctory matter or as a joke. He is under no duress from the insurance company in correcting an erroneous charge such as an employee would be. On the other hand, if he is fined for not correcting it he will have to stand the punishment himself, while the witness Tabb expressed the opinion that, if a branch manager should be fined for carrying out his employer's orders, *the company would stand it*. Mr. Tabb has been in the business nearly half a century and has had enough experience to form an intelligent opinion. But be that as it may, the branch manager has not taken the duty of countersigning at all seriously, and it should not longer be entrusted to him.

The statutes referred to impose a heavy responsibility on the resident commission agent to see to it that the insurance company does not violate the Virginia laws in the issuance of policies as well as in other transactions in relation thereto, for he is a participant in these transactions. The branch manager appellants certainly have no vested constitutional right to treat a serious legal obligation of this kind as a joke, as they have treated their countersigning duties.

The appellants contend that the provision preventing the Virginia commission agent from paying any part of

his commissions to an unlicensed nonresident broker is unconstitutional as undertaking to extend Virginia's regulatory powers over insurance brokers' actions in other states. But this provision is not a regulation of the nonresident broker, it is a regulation of the Virginia licensed resident agent. Section 4226a contains the following provision:

> "No regularly constituted and registered resident agent or agency for any insurance company shall sign or countersign any blank contract of insurance or surety; nor may such *resident agent* or agency allow or *pay to any agent not regularly commissioned and registered, or to any unlicensed non-resident insurance broker any portion of any commission which he receives or is entitled to receive*" (Virginia Code section 4226-a).

It will be observed that the agent cannot pay an *unlicensed Virginia agent* any part of his commission. Can any good reason be advanced why he should give preferential treatment to an *unlicensed nonresident broker?* Or, if he can pay part of his commission to such unlicensed broker why he cannot pay it as a rebate to a nonresident assured?

It is submitted there is no merit in either of the contentions above referred to.

Similar Statutes in Other States

The Virginia statute, requiring insurance companies licensed to do business in Virginia to make contracts of insurance or surety on persons or property in Virginia through regularly constituted and registered resident agents, is not unusual at all. Resident agent statutes, in

one form or another and with varying degrees of application, exist in all of the forty-eight states. It might be helpful to call attention to some of these enactments.

Appellants' witness Haas, the assistant attorney of the Association of Casualty and Surety Executives, testified that he had made a study of the laws of the respective states relating to resident agents, so far as such laws affected the casualty and surety business. He found that in the states of Louisiana, Mississippi and North Carolina there were statutes raising problems comparable to that of Virginia (R. 204-5). This witness also referred to somewhat similar situations resulting from statutes in Montana, Oklahoma, Rhode Island, South Dakota, Washington, Wisconsin and Wyoming.

To illustrate the operation of these resident agent laws, the Court's attention is called to the following additional insurance statutes, to indicate the nature of these statutes generally:

A South Carolina statute, section 7954 of the Code of Laws of 1932, was construed by her Attorney General as requiring countersignature by a resident commission agent and payment to him of full commissions.

In ALABAMA it is provided in Section 289:

> "To facilitate collection of premium taxes and fees for agents, all stock fire and casualty insurance companies doing business in this State shall issue all policies upon property or risks in this State through resident agents, duly licensed, who shall countersign all policies. Each agent shall collect and retain the usual commission paid by the insurers except that not over one half of such commission may be paid to a licensed non-resident agent or broker * * *."

There is also a revenue law in Alabama known as Schedule 160.15, as follows:

"To assure the validity and construction of contracts according to the laws of this state, and to facilitate the collection of privilege taxes and fees for agents, all fire, surety and casualty insurance companies doing business in this state shall execute all contracts upon property or risks in this state through resident agents, duly licensed, who shall execute or countersign all such contracts. No special agent shall execute or countersign contracts. Each agent shall collect and retain the usual commission paid by the insurer except that not over one half of such commission may be paid a licensed non-resident agent or broker * * *. Non-resident agents, and non-resident brokers must also be licensed and shall pay an annual license of $25.00, but shall not execute or countersign fire, surety, or casualty insurance contracts. Special agents, both resident and non-resident, shall also be licensed, but shall not execute or countersign fire, surety or casualty insurance contracts * * *."

In ARKANSAS, Section 345 (7957) provides:

"No fire, accident, steam boiler, employers' liability, surety or workmen's compensation or other casualty company, shall assume liability, either under direct policies or by reinsurance, in its line of this State, except by and through a duly authorized and commissioned resident agent in this State."

In CALIFORNIA, Section 801 states:

"Except as provided by this article, an admitted insurer shall not cause to be executed or renewed any contract of insurance covering subject matter

located in this State at the time of execution or renewal, except either (a) through a resident agent, or (b) after approval in writing by such an agent."

In COLORADO, Section 2510 (40) provides:

"It shall be unlawful for any foreign insurance company to make, write, place or cause to be made, written or placed in this state any insurance policy or contract of any kind to provide against any contingency which may be insured or guaranteed against, unless done through its duly and regularly appointed and authorized agent or agents, residents of this state * * *."

And Section 2535 (65) of the same Colorado law provides:

"No foreign fire or casualty insurance company doing business in this state shall make, write, place or cause to be made, written or placed any policy, duplicate policy or contract of insurance of any kind or character or any general or floating policy, upon persons or property resident, situated or located in this state; except after the said risk has been approved, in writing, by an agent who is a resident of this state, regularly commissioned and licensed to transact insurance business herein, who shall countersign all policies so issued and receive the full commission thereon when the premium is paid."

In CONNECTICUT, Section 4121 provides:

"No non-resident or foreign insurance company shall issue or deliver any policy or make any contract of insurance on either persons or property in this state, or covering any hazard or risk in the performance or non-performance of any duty relative to any

contract or obligation, performed or to be performed in this state, or in connection with any obligation or duty which is governed or controlled by the laws of this state, but actually to be performed by any individual, firm or corporation not resident in this state, unless such policy or contract is issued through and countersigned by a lawfully constituted and licensed resident agent of this state * * *."

In DELAWARE, it is provided in Section 588 (17):

"No foreign or alien insurance company, other than a life insurance company, shall make, write, place or cause to be made, written or placed, any policy, duplicate policy, or contract of insurance of any kind or character, or any general or floating policy upon property situated or located in this state, except after the said risk has been approved in writing by an agent who is a resident of this state, regularly commissioned and licensed to transact insurance business herein, who shall countersign all policies or contracts so issued, and who shall receive the full premium paid thereon and the state shall receive the taxes required by law to be paid on the premiums collected for insurance on all property located in this state."

In ILLINOIS, it is provided in Section 22 of the 1936 Act providing for the licensing of Insurance Agents:

"No policy of insurance or contract of fidelity and suretyship covering property or risks in this State shall be issued unless and until such policy or contract or the written application therefor shall have been countersigned by a duly licensed resident agent."

In INDIANA, Section 216 provides:

"Only agents who are residents of this state, or whose principal office for the conduct of such agency is maintained in this state, shall as agent, solicit, negotiate or effect contracts of insurance, or sign, countersign or issue any policy of insurance for or on behalf of any insurer, on any property, or insurable business activities or interests, located within, or transacted within this state."

In IOWA, Section 8943-e1 states:

"No insurance company admitted to do business in this State shall write, place or cause to be written or placed any policy or contract of insurance covering risks located or situated in this State, or any contract or indemnity or suretyship, except through or by a duly licensed agent of such company, residing within this State and licensed by the Commissioner of Insurance of this State."

In KANSAS, Section 40-246 provides:

"* * * To the end that the state may receive the full tax imposed by law upon the premium receipts of insurance companies, and to the end that proper supervision of the business may be vested in the State, it shall be unlawful for any fire, marine or fire and marine insurance company or casualty or surety company or association not incorporated under the laws of this State to make, write, place or cause to be made, written or placed any policy or contract of insurance of any kind or character or any indemnity agreement upon property or persons situated in this State unless the same is signed by a resident agent of this State regularly commissioned and licensed as such, who shall receive the usual and

customary commission thereon when the premium is paid."

In KENTUCKY, Section 762A-20 of Subdivision IX provides:

"No insurance company shall write, place or cause to be written or placed, any policy or contract for direct insurance upon any property in this Commonwealth, except through a duly licensed resident local agent in this Commonwealth; provided, however, the words duly licensed resident local agent, as used in this section, shall not be construed to mean or to include, in any sense, any State or special agent or travelling and/or salaried employee of any stock fire insurance company doing business in this Commonwealth * * *."

In MARYLAND, Section 65 provides:

"No company authorized to transact business in this State, and no person, resident or non-resident, shall write any policy of insurance, or assume any liability in the matter of insurance upon any property, real or personal, situated in this State, unless such policy, certificate or other evidence of liability assumed by said company or person shall have been, previous to delivery, signed or countersigned by an officer or agent, resident in this State, authorized by law to sign such policy or contract; provided, however, that policies issued to railway corporations insuring the rolling stock and other movable property of said road, and those insuring the liability of such railroads as common carriers, shall be subject to the requirement that they shall be signed by the resident agent in cases only where more than one-half the trackage of the roads operated by such railway companies is situated in the State of Maryland.

Every company or person, resident or non-resident, engaged in business in this State, shall pay to its legally licensed agent in the State of Maryland, for signing or countersigning any policy, certificate or other evidence of liability assumed by said company or person the same rate and amount of commission as if such policy, certificate or other evidence of liability, had been issued through said agent residing in the State of Maryland; and no agent shall sign or countersign any policy, certificate or other evidence of liability, upon any property situated in this State, for an amount less than the commission allowed on any policy, certificate or other evidence of liability issued through an agent residing in this State. The premiums on all policies so signed or countersigned shall be included in the report of gross premiums required to be made to the Insurance Commissioner by all companies not organized under the laws of this State."

In MASSACHUSETTS, Section 157 provides:

"Foreign companies admitted to do business in the Commonwealth shall make contracts of insurance upon lives, property or interests therein, and annuity or pure endowment contracts with residents thereof, only by lawfully constituted and licensed resident agents."

In NEW YORK, Section 69-a provides:

"No insurance company or insurer organized or existing under the laws of any other state or country shall issue or deliver any policy or make any contract of insurance * * * unless such policy or contract is issued through or countersigned by a lawfully constituted and licensed resident agent of this state * * *."

Section 142 of the New York law provides:

> "1. The term 'agent' in this section shall include an acknowledged agent or any person, partnership, association or corporation who shall in any manner aid in transacting the insurance business of any underwriter, incorporated or unincorporated, by negotiating for or placing risks or delivering policies or collecting premiums, but shall not include the officers and salaried employees of any such underwriter, who do not receive commissions."

Section 143 of the New York law deals at considerable length with the operation of brokers in that state. Paragraph 2 of that section provides:

> "No underwriter, authorized or permitted to do business in this state, or agent thereof, shall pay any money or commission or give or allow anything of value to any person, partnership, association or corporation not a duly authorized agent of such underwriter for or because of his or its negotiating a contract of insurance or placing a risk or taking out insurance or a surety bond, unless such person, partnership, association or corporation is authorized to act as a broker. No person * * * shall act as broker * * * without first procuring a certificate of authority so to act from the superintendent of insurance."

Paragraph 14 of the same section states:

> "If, by the existing or future laws of any other state, any broker resident within this state and duly licensed as such under the provisions of this section, may not be licensed as a broker in such other state, then no broker resident in such other state shall be licensed as a broker within this state, anything in

this section to the contrary notwithstanding. If * * * the amount of commissions which may be paid to such broker on premiums on risks located in any other state shall be limited under the laws of such state, then and in every such case, all brokers resident in such other state shall upon being licensed in this state pay a like fee in lieu of that prescribed by this section, and insurance companies which are authorized to transact business in this state shall not pay to any such non-resident broker any commissions on premiums on risks located in this state in excess of the commissions which the laws of such other state permit brokers of this state to receive on premiums on risks located in such other state."

The above statutes cited are illustrative of the variety of statutory provisions now in effect in all the states with reference to the operation of foreign insurance companies through licensed resident agents.

VIII.

This Case is not Controlled by Hartford Steam Boiler Inspection and Insurance Company v. Harrison[1]

Appellants' brief does not discuss this case (which will be referred to herein as the *Harrison case*), nor did appellant rely on same in the District Court. However, that Court thought the cases so similar that it requested the filing of briefs discussing the case and its effect, if any, on these Virginia statutes. The case will therefore be discussed here for the Court's use should it be deemed proper for consideration.

The *Harrison case* was instituted by a petition for mandamus filed by the Insurance Company and one of its salaried employees to compel the Georgia Insurance

[1] 301 U. S. 459, 81 L. ed. 1223.

Commissioner to issue said employee a license as an insurance agent for the writing of casualty insurance. The only reason the license was refused was because of the provisions of the Georgia statute prohibiting salaried employees of stock surety, casualty, or fire insurance companies from being licensed as insurance agents, but permitting salaried employees of mutual companies to be so licensed. The county court granted the mandamus, the Supreme Court of Georgia reversed, and this Court in turn reversed the latter.

The Georgia Statutes Involved

Section 56-508 of the Code of Georgia, as amended by an Act approved March 28, 1935, contained these provisions:

> "No licensed fire or casualty insurance company or company writing fidelity or surety bonds, shall write or issue any policy or indemnity contract on any risk in this State *except through a resident agent licensed by the Insurance Commissioner;* Provided that no contract bond shall be issued by any company, except through an agent, resident of the county in which the work under contract is located, if the company has an agent, resident in the county in question. The full commission thereon (meaning thereby the commission paid for the production of business by him), shall be paid to such resident agent. *Provided, however, that such resident agent may pay a commission on business placed with him by another duly licensed resident agent, and, provided further, that such resident agent may pay a commission not exceeding fifty per centum of the regular commission allowed resident agents upon the issuance of such policies or contracts, to a duly licensed non-resident on any business originated by such non-resident.* This section shall not apply to policies covering property in transit while

in the custody of any common carrier or to rolling stock of any common carrier, nor to cotton insurance issued under a per bale reporting form of coverage. *The words 'resident agent' as used in this section are deemed to mean resident agents engaged in the solicitation of such business from the public generally and shall not include any salaried employee of any insurance company doing business in this State; but shall include any agents of mutual insurance companies however compensated. * * *.*" (Italics supplied.)

The above italicized definition of "resident agent" prohibited any salaried employee of stock companies from engaging in the solicitation of surety, casualty or fire insurance contracts. At least this is the construction apparently given the Act by this Court.

THE VIRGINIA STATUTE DISTINGUISHED

The controlling distinction between the Georgia statute involved in the *Harrison case* and the Virginia statute here involved lies in the acts which they severally permitted salaried employees of stock companies to perform. It was the prohibition against the Georgia salaried agent of stock companies engaging in doing any of the acts of "agents engaged in the solicitation of such business from the public generally" which was held to be unreasonably and arbitrarily discriminatory. In other words, salaried stock agents could not engage "in the solicitation of such business from the public generally" because this function was restricted solely to, and was the test of what constituted, a "Resident Agent" in Georgia, and a "Resident Agent" could not be compensated by salary. The effect of this was obviously to wholly exclude the

branch manager or other salaried officer or employee of a stock company from the production field.

Now the Virginia statute is exactly the opposite in its provisions and in its effect. So far from excluding those on salaries from the production field, the statute (Sec. 4221-a) contains the following definition of them, which includes the appellant branch managers:

> "'State agent', 'special agent' or 'company representative' means any person, who *acts* in this State for or on behalf of any insurance company or other insurer, in the *solicitation, inspection or servicing* of risks assumed or to be assumed by said company; provided this definition shall not apply to life insurance companies, except the casualty branches of such companies." (Italics supplied.)

Thus the salaried stock special agent or employee may "act" for his company, (1) in the "solicitation," (2) in the "inspection," and (3) in the "servicing" of risks. These three activities cover the entire production field, so it is pertinent to inquire in what respect the stock company is restricted in Virginia from acting through such salaried agent or employee.

What the Virginia Stock Salaried Agent or Employee is Prohibited from Doing by the Virginia Statute

The only two functions which such an agent or employee may not perform are the following:

(1) He may not be paid any part of the "customary commissions" paid to commission agents,—generally known as the "producers' commission"—which is a factor in the premium rate of stock companies. Of course, there is nothing to prohibit the stock company from pay-

ing him commissions if it desires to do so, provided it pays the "producers' commission" to a "Resident Agent."

(2) While he may sign contracts for his company, he may not provide that requisite *"countersignature"* which must be furnished by a "Resident Agent" in order to make the contract legally effective.

In all other respects, the stock salaried agent or employee may do any act on behalf of his company in soliciting, servicing or inspecting risks which the salaried agent of the mutual company may do. *In fact, the only act which a Virginia mutual company may do through its salaried agent or employee which a stock company may NOT do is to have its contract validated by such an agent's or employee's countersignature.*

The Questions Involved in the Harrison Case

The opinion of the Supreme Court of Georgia, as well as the digest of appellants' brief in the Supreme Court of the United States, as reported in the Lawyer's Edition, show that the petition in the *Harrison case* challenged the Georgia statute upon the following grounds:

(1) That the statute was (to quote from the Georgia opinion, 187 S. E. 648, 650-51)

> "* * * violative of the Fourteenth Amendment to the Constitution of the United States, in that said provision is arbitrary, unreasonable, and capricious, and bears no reasonable relation to the public or to any other matter or thing within the police power of the state, and deprives the petitioners of their property and of their liberty, without due process of law; * * *"

(2) "* * * that said statute, in discriminating against stock companies and the agents thereof and

> in favor of mutual companies and the agents thereof, sets up an arbitrary and capricious classification bearing no reasonable relation to the subject-matter of the legislation, and no reasonable relation to the protection of the public, or any other matter within the legislative authority; * * *."

The majority opinion did not discuss the due process question, but the four dissenting justices were "of the opinion that its [the Supreme Court of Georgia's] decision was right and should be affirmed." It is not unreasonable to conclude that a majority of the court were unwilling to declare the statute unconstitutional on the ground that it violated the due process clause. In this connection it is significant that the Georgia statute contained a provision, similar to that in Virginia here challenged, requiring all the commissions to be paid to the resident agent and limiting such agent from paying more than fifty per cent thereof to a duly licensed nonresident agent or broker on business originated by such nonresident. This particular statutory provision, which with the countersignature requirement are the only complaints now being urged upon this court, did not seem to impress this Court as arbitrary, capricious or unreasonable or as denying due process. It was in no way adversely commented on or criticized by that court.

It was upon the second ground alone,—that the statute was unreasonably discriminatory and violated equal protection as between stock and mutual companies,—that this Court rested its decision.

What the Harrison Case Decided

The opinion is rested solely on the conclusion that, upon the record before the court in that case the majority

of the court could "discover no reasonable basis for permitting mutual insurance companies to act through salaried resident employees and exclude stock companies from the same privilege. If there were any such basis, it would have been discovered by the state courts." "* * * the appellant company had been licensed to do business in the State and was entitled to equal protection in conducting that business" (301 U. S. at p. 463). In other words, neither the *facts* contained in the record in that case nor *facts* existing in Georgia and within the judicial cognizance of the court supplied any sufficient reason for the distinction between the manner in which mutual and stock insurance companies were required to conduct their business in Georgia under the Georgia statute, which entirely excluded stock company salaried employees from the production field.

It appears from the opinion of the State Court (187 S. E. at p. 651) that no evidence was taken in the *Harrison case*, but that mandamus was awarded upon the pleadings alone, which consisted of the petition and the insurance commissioner's answer. The answer, so far as appears from the opinions of both courts, seems to have been barren of *factual* allegations, merely averring that there was a wide difference between mutual and stock companies. Nor does the opinion of the Georgia Supreme Court disclose any *facts* as to the customs and practices in Georgia relating to the insurance business, or which would tend to support the classification of mutual and stock companies so as to prohibit the latter from *soliciting business* through salaried branch managers or special agents. In fact, it is difficult for anyone to conceive of a sound basis for denying them this

privilege. Certainly, as has been pointed out, the Virginia statute contains no such prohibition.

The Supreme Court's opinion in the *Harrison case* seems to have viewed the Georgia statute as not only prohibiting the stock companies from *soliciting* through *salaried* agents and employees, but from doing *any other act* through them. The court said it could "discover no reasonable basis for permitting mutual insurance companies *to act* through salaried resident employees and exclude stock companies from the same privilege." Certainly there is no intimation in the opinion that the only function the salaried mutual agent could perform which the stock agent could *not* was restricted to *"countersigning"* contracts. Nor would there have been any foundation for any such intimation, because neither the word "sign" nor "countersign" appears in the statute or in the opinion of either court. If the classification of the acts permitted to be done through their salaried agents by stock and mutual companies, respectively, had been restricted by the Georgia Statute to this one act of countersigning, it is most probable that evidence would have been taken to prove facts to justify it, as was done here.

It is clear, therefore, that the decision in the *Harrison case* dealt with a question essentially different from that here involved and that it has no application to this case at all.

A. Whether the Statute is Unduly Discriminatory and Therefore Denies Equal Protection is a Factual Question.

A claim of denial of equal protection is necessarily based upon *facts*. The first questions which arise are: Equal protection from what? In what respect is the complainant being discriminated against? If there is discrimination, this alone does not constitute a denial of

equal protection, but it must be an unreasonable and arbitrary discrimination, so why is this discrimination unreasonable and arbitrary? In what respect and to what extent is the complainant injured? The answers to all these questions in this case involve facts relating to the respective customs and practices of the mutual and stock companies.

The *Harrison case* does not hold that the inherent differences between mutual and stock insurance companies, their customs and practices do not afford a basis for *any* distinctions or differences in regulating them. Obviously there must be differences. A regulation based upon a classification of salaried agents and commission agents of companies which employ both would be incongruous and meaningless if sought to be applied to a company which does not employ commission agents at all. A regulation as to the payment of the commission factor of a stock company insurance premium could not be applied at all to a mutual premium which has no commission factor in it to be paid to any one. A regulation prohibiting a stock insurance company from engaging in a practice it has never engaged in, and has no desire to engage in,—*e.g.*, paying commissions to its salaried employees,—cannot be either injurious to said company or unreasonable. A regulation as to the payment of the producers' commission factor of a premium, designed to remedy an evil of rebating part of the commission, would have little, if any, relation to a mutual company which pays commissions at such a small rate that the agent cannot afford to give any rebate.

A regulation, however, which excludes all salaried agents and employees from the insurance production field entirely, as in the *Harrison case*, could have application to all companies whether mutual or stock, and is

obviously very far reaching in its effect. When applied to stock companies only, it places the company in a position of complete dependence upon the good will and favors of the commission agent, who may represent several companies. Obviously, this should not be. But in Virginia the branch managers, special agents and other salaried company representatives may solicit business. When they solicit business it is usually in the capacity of assisting their commission agents and even if they negotiate contracts alone the invariable practice of the plaintiff companies has always been to close the contract through a commission agent and pay him the producers' commission, which is all that the Virginia statute requires (Op. R. 47).

And so, the decisions of this Court, in determining whether a statutory regulation is arbitrarily discriminatory and denies equal protection, invariably apply the *specific regulation involved* to the facts and circumstances as reflected in the existing customs and practices to which the regulation is applied.

The most recent decision as to the proper test for determining the constitutionality of state statutes classifying subjects of taxation or regulation is *Clark* v. *Paul Gray*, 306 U. S. 583. The case involved the validity of a California statute imposing a tax upon automobile caravans driven on the highways, one objection urged being a deprivation of equal protection because automobiles transported singly or in one zone, or caravans driven within one zone, were not taxed. This, it was contended, was an unreasonable and arbitrary classification, and denied equal protection. The case turned upon a question of fact,—whether automobile caravans were more dangerous or more destructive to the highways than those driven singly. This Court said:

"* * * It is true that the district court found that the practice of caravaning creates no additional traffic hazard, nor any undue wear and tear on the highways. But in this we think that its determination was not only contrary to the evidence, *but went beyond the judicial province.*

"It is no longer open to question that the states have constitutional authority to exact reasonable fees for the use of their highways by vehicles moving interstate, [citing authorities] and that for that purpose they may classify the vehicles according to the character of the traffic and the burden it imposes on the state by that use, and charge for the use a fee not shown to be unreasonable or excessive. [Citing authorities].

"The classification of the traffic for the purposes of regulation and fixing fees is a legislative, not a judicial, function. Its merits are not to be weighed in the judicial balance and the classification rejected merely because the *weight of the evidence* in court appears to favor a different standard. Cf. *Worcester County Trust Co.* v. *Riley*, 302 U. S. 292, 299, *The determination of the legislature is presumed to be supported by facts known to it, unless facts judicially known or proved preclude that possibility. Standard Oil Co.* v. *Marysville*, 279 U. S. 582, 584; *Borden's Farm Products Co.* v. *Ten Eyck*, 297 U. S. 251, 263; *South Carolina State Highway Dept.* v. *Barnwell Bros.*, 303 U. S. 177, 191, 192; *United States* v. *Carolene Products Co.*, 304 U. S. 144, 153, 154. Hence, in passing on the validity of the present classification, it is not the province of a court to hear and examine evidence for the purpose of deciding again a question which the legislature has already decided. *Its function is only to determine whether it is possible to say that the legislative decision is without rational basis.* This is equally the case where the classification, which is one which the legislature was competent to make, is applied to

> vehicles using the state highways in interstate commerce. *South Carolina State Highway Dept.* v. *Barnwell Bros., supra.* The legislature must be assumed to have acted on information available to courts, and where, as here, the evidence, like that discussed in *Morf* v. *Bingaman*, 298 U. S. 407, *supra*, shows that it is at least a debatable question *whether the traffic in caravans involves special wear and tear of the highways and increased traffic hazards* requiring special police control, decision is for the legislature and not the courts. * * *" (Italics supplied. 306 U. S. at pp. 593-4).

The controlling factual question is stated in the language last above italicized: It is apparent from the foregoing quotation and the cases cited therein, that a claim of denial of equal protection is one to be determined solely by the *facts*, that there is a very strong, though rebuttable, presumption that the requisite facts do exist, and that the burden is on him who claims denial of equal protection to *both allege and prove the facts* which are relied on to sustain the claim that the statutory regulation is without rational basis and that he is injured thereby.

The necessity of the Court having before it the facts bearing upon a constitutional question of this nature in order to properly decide it is emphasized in the first decision in *Borden's Farm Products Co.* v. *Baldwin*, 293 U. S. 194, which involved the question whether there was a rational basis for fixing the price of well advertised brands of milk at a higher price than brands not so advertised. The case was heard in the lower court on bill and answer, and the bill dismissed. The Supreme Court, in remanding the case for the taking of evidence and the finding of facts, said:

"* * * It is not a conclusive presumption, or a rule of law which makes legislative action invulnerable to constitutional assault. Nor is such an immunity achieved by treating any fanciful conjecture as enough to repel attack. When the classification made by the legislature is called in question, if any state of facts reasonably can be conceived that would sustain it, there is a presumption of the existence of that state of facts, and one who assails the classification must carry the burden of showing by a resort to common knowledge or other matters which may be judicially noticed, or to other legitimate proof, that the action is arbitrary. * * *" (293 U. S. at p. 209).

After evidence had been taken pursuant to the Supreme Court's direction in the above case, and the District Court had made its findings of fact and dismissed the bill upon the merits, the case was again heard by the Supreme Court (297 U. S. 251). In affirming the dismissal, Mr. Justice Roberts, after an elaborate analysis of the facts, stated the legal principles applicable, and as they are peculiarly pertinent here they will be quoted for the convenience of the Court:

"We hold that the fixing of the differential in favor of the sellers of milk not having a well-advertised trade name, *in the situation exhibited by the findings*, does not deny the appellant equal protection.

"The argument is that the classification is arbitrary since the statute puts the appellant and other dealers who have well advertised trade names in a single class solely by reason of the fact that their legitimate advertising has brought them good will. So, it is said, they are penalized for their business skill and acumen. The answer seems sufficiently obvious. In enforcing its policy of price fixing,—a temporary expedient to redress an injurious economic

condition,—the legislature believed that a fixed minimum price by dealers to stores would not preserve the existing economic method of attaining equality of opportunity. That method was for the well-advertised dealers to rely on their advertising to obtain a given price, and for the independents to retain their share of the market, *not* by *counter-advertising* but by a slight *reduction of price*. The one expedient the law did not purport to touch; the other by fixing the same minimum for all dealers it would effectually destroy. In these circumstances, it was competent to the lawmakers to attempt, during the limited term of the legislative experiment, to preserve the *existing* relationship of advantage established by the *past trade practices* of the two groups. So to do, we must assume, was within the legislative power under the state constitution. No prohibition of the expedient is found in the federal Constitution, unless in the Fourteenth Amendment. We have held that article does not prevent the fixing of maximum and minimum prices for milk, *in the circumstances existing in the State of New York in 1933*. We now hold that to provide that a differential of one cent maintained by the independent dealers shall *continue* does not deny their advertised competitors equal protection. There was a plain reason for the classification. It was not merely that appellant had established a good will; it was that *there had resulted* a balance between that advantage and the resulting disadvantage to the unadvertised dealer,—a balance maintained by a price differential. To attempt the maintenance of that balance was to strive for equality of treatment, equality of burden, not to create inequality. *To adapt the law to the existing trade practice was neither unreasonable nor arbitrary.* The present case affords an excellent example of the difficulties and complexities which confront the legislator who essays to interfere in sweeping terms with the natural laws of trade or industry. The dan-

ger in such efforts always is that unintended dislocations will bring hardship to groups whose situation the broad rules fail to fit. Where, as here, there is recognition of an *existing status* and an attempt to equate the incidence of the statute *in accordance with it*, we find a compliance with, rather than a disregard of, the constitutional guaranty of equal protection. *The appellant cannot complain if, in fact, the discrimination embodied in the law is but a perpetuation of a classification created and existing by the action of the dealers.* In the light of the *facts* found the legislature might reasonably have thought trade conditions existed justifying the fixing of a differential. Judicial inquiry does not concern itself with the *accuracy* of the legislative finding, but *only* with the question whether it *so lacks any reasonable basis* as to be *arbitrary*. *Standard Oil Co.* v. *Marysville*, 279 U. S. 582, 586, 587, * * *; *Borden's Farm Products Co.* v. *Ten Eyck*, 297 U. S. at pp. 261-3. Italics supplied.)

It is respectfully submitted, therefore, in conclusion on this point, that the question whether, in a case of this nature, the plaintiffs have been denied equal protection under the Fourteenth Amendment is a factual question, dependent upon whether the statute is appropriately adapted to existing insurance practices of the stock and mutual companies, respectively.

B. Factual Conditions in Virginia and Georgia are not Necessarily the Same

As heretofore pointed out the Virginia statute here attacked is essentially different from the Georgia statute involved in the *Harrison case*. But even if they were the same, an adjudication of the fact that insurance conditions and practices existing in Georgia in 1935 did not afford a rational basis for that state's classification of

mutual and stock insurance companies at that time in that state could not be considered an adjudication of the very different fact that conditions, customs and practices in Virginia, and in New York affecting Virginia, existing in 1939, are inadequate to provide a rational basis to support same. The decisions of this Court clearly show that a statute which, under facts and circumstances existing at one time, is deemed to be constitutional or unconstitutional, may be held the reverse at another time under changed conditions even in the same state. *Chastleton Corp.* v. *Sinclair*, 264 U. S. 543, 68 L. ed. 841, and cases cited.

In the second *Borden Case, supra,* the Court, while holding that the facts proven were not sufficient to require a conclusion that the classification was without rational basis, nevertheless was careful to point out that the Borden Company had the right to have redress from the courts in the future "if there were proof that in practice it produces such gross inequality, and so unnecessarily damages the plaintiff as to shock the conscience." It is clear, therefore, that the question whether the appellants here are deprived of equal protection by the Virginia statute involves an essentially different factual situation in a different part of the United States, from that involved in the *Harrison case,* and that this Court cannot base its decision in this case upon the assumption that the factual conditions are the same in Virginia now as they were in Georgia in 1935. Obviously, a valid regulation governing the sale of ice or milk in Florida during the winter months might be grossly unreasonable and arbitrary in the State of Maine.

As stated, the adjudication of factual conditions in Georgia in the *Harrison case* cannot be said to constitute a decision, or even be authority for the proposition, that

the facts are the same now in Virginia; nor can said decision be an authority for the proposition that facts do not exist in Virginia now which afford a reasonable basis for the essentially different Virginia statute. The only similarity in the statutes is a superficial one.

C. The Facts Proved Justify Exempting Mutual Companies from the Virginia Statute

The only distinction drawn by the Virginia statutes between mutual and stock companies, their agents and employees is that the stock company must pay the commission factor of its premium to a commission agent and not to a salaried employee, and that the commission agent shall countersign the contract of insurance. Since, (with immaterial exceptions), mutual companies do not have commission agents, and do not have a commission factor in their premiums and do not pay any "customary commissions" to anyone, the statute would be meaningless if mutuals were included, unless the statute were extended to *require* mutuals to operate on an entirely different principle. The appellees do not believe the stock companies would desire any such requirement. They are vigorous in their arguments that the assured receives greater value for his money in a stock company policy than in a mutual, and the chief reason they give for this is the superior service rendered by the impartial commission agent. Thus, in the address of the Assistant General Manager of the Association of Casualty and Surety Executives, (quoted *supra*, pp. 32-4) we find the following:

> "'*The only medium through which this service can be rendered consistently is the agent in the field.* He is less the representative of the company whose

policies he places than he is the representative of the individual or company he insures. *The capital stock agent is not a salaried employee who must respond to the direction of any one company or group of companies.* He is a business man, doing business in his own local community. His first consideration must be his clients. *That means greater protection for the public than is possible in the case of the direct-writing mutual which operates through a salaried employee*'."

And in the address of the Vice-President of the American Insurance Company, (quoted *supra*, pp. 100-101), the speaker contrasted strongly the superior service rendered by commission agents over salaried solicitors and concluded with these words:

"'* * * and *that account is not subject to attack by direct-writing companies, nor by mutual and reciprocal carriers, even though they pay alluring dividends*'."

And just as *mutuals* do not pay *commissions*, so, on the other hand, *stock companies* do not pay *salaries* to their *commission* agents, or *commissions* to their *salaried* officers and employees.

This distinction in the customs and practices of mutuals and stock companies is fundamental. The commission agent has a much stronger incentive to produce business than a salaried employee, because the business, when produced, is his business and he expects to keep it on his books. There is a definite salable value in his prospects of renewals, and the stock company recognizes his ownership of it. On the other hand, the mutual salaried employee, if discharged, owns no interest in the business he has produced. It belongs to the mutual company.

This powerful incentive which the commission agent has to produce business, and the service he renders his client to retain it, no doubt furnish the reasons why the stock companies write many times as much business as the mutuals. The last thing the stock companies would wish would be a statute requiring mutuals to pay commissions and provide the same powerful motivating incentive to their agents. The mutual salaried solicitor sells at a smaller premium, it is true, but because of his lack of incentive produces less business and, the stock companies assert, renders less service to the assured.

This fundamental and basic distinction in the principles upon which mutual and stock companies operate is reflected in their premium rates. All stock company premiums include a factor to provide for the payment of commissions.

But the mutuals have no such factor in their rates. Their assureds do not buy or pay for the services of an impartial commission agent but they pay less for their insurance. There would be no point to applying this statute requiring countersignature by a commission agent to a mutual company which has no such agent and whose assured pays no such commission in his premium. On the other hand, the stock company assured does pay such commission in his premium and one of the purposes of the statute is to see to it that he gets the impartial service he pays for. An important part of this is rendered at the time of countersigning.

The opinion in the *Harrison case* emphasizes that it could "discover no reasonable basis for permitting mutual companies to act through salaried resident employees and exclude stock companies from the same privilege". The Virginia statute only excludes stock company salaried

employees from countersigning contracts and receiving commissions. It does not exclude the stock company from acting through them in any other respect.

And there is every good reason shown in this record why stock company salaried employees should do neither. As to receiving commissions, the appellants themselves have recognized and acted upon the sufficiency of the reason by adopting an invariable practice of refraining from paying them to their salaried officers and employees, as the appellants admit in their brief (p. 12). In addition, the commission factor of the premium is, by custom, dedicated to the payment for the services of an impartial agent, and it would be inconsistent and violative of good faith to pay it to a salaried employee of the insurer.

The question whether there is a reasonable basis for the requirement that resident commission agents must countersign contracts, as well as receive the commissions, has been fully discussed at pages 68-113, *supra*. There are discussed the harmful practices incident to hotchpotch contracts, rebating by New York brokers and by the stock insurance companies on contracts made outside of Virginia, and the unfair competition resulting therefrom in discrimination against Virginia agents and Virginia insurance companies, as well as against Virginia industrialists, merchants, property owners and business men generally. Also, is discussed the legitimate and proper purpose of the act to secure to assureds the benefit of the services of a local resident impartial agent. The basis which would support the reasonableness of the statute as against the appellant's challenge also would support it as against a charge of arbitrary and unreasonable discrimination, because the evils sought to be remedied are not found in the practices of the mutual companies. There are few, if any, mutual "groups," con-

taining parent, subsidiary and affiliated companies engaged in the separate lines of surety, casualty and fire insurance, and they do not combine these numerous types of risks in one hotchpotch contract. Mutual agents do not rebate commissions because they do not receive any. (While there is an immaterial exception to this last statement, in that two or three of the several thousand mutual companies do pay commissions, the commission is so small as not to permit effective rebating. See the dissenting opinion in the *Harrison case.*) Mutuals do not rebate premiums, they pay a dividend, and never discriminate as between their policyholders. In fact, as above pointed out, the testimony of appellants' New York broker witnesses indicates that the brokers do little, if any business with the mutuals. They present no field for the exercise of the broker's auctioneering talents. He cannot secure any rebates or reduced premium rates, hence there is no need for his services in negotiating contracts with mutuals. Again the mutual assured has no commission included in his policy and therefore does not pay for the services of a commission agent, so there would be no basis for a requirement that such an agent countersign or be associated with his contract, and there is no evidence that the two or three mutual companies who do pay commissions do not associate their Virginia commission agents with the contracts, if any, which they make outside of Virginia, or that such agents are not paid full commissions therefor.

Furthermore, there is no evidence of any need for a Virginia commission agent to countersign mutual policies in order to assist in policing the mutuals to prevent violation of premium rates fixed by Virginia law, whereas, the stock companies assert in their brief in this case that Virginia has nothing to do with rates they

charge for Virginia coverage contracts made outside the State. The chief evils sought to be remedied by this statute,—*i.e.*, rate cutting and rebating on Virginia coverage contracts negotiated outside the State, and securing to the assured the services of a Virginia impartial commission agent—are not found in the practices of the mutual companies. They do not indulge in rate cutting or rebating and their assureds do not pay for the services of an impartial commission agent; their insurance costs them less so they are not entitled to this service.

D. The Test of Reasonableness, from the Standpoint of Denial of Equal Protection, is Whether the Statute is Appropriately Adapted to the Existing Practices of Mutual and Stock Casualty Companies, Respectively.

The second *Borden's Milk case* (297 U. S. 251), as has been pointed out, involved the question whether a statute fixing the minimum price at which advertised brands of milk could be sold at one cent greater than brands not so advertised. The Borden Company, which advertised its milk, complained that this discrimination was unreasonable and denied it equal protection. But the evidence showed that it was customary for the non-advertisers to charge one cent less, and in view of this practice, the court said:

> "* * * The appellant cannot complain if, in fact, the discrimination embodied in the law is but a perpetuation of a classification created and existing by the action of the dealers. * * *." (297 U. S. 263.)
>
> "* * * To adapt the law to the existing trade practice was neither unreasonable nor arbitrary. * * *." (297 U. S. 262.)

Applying this principle to the Virginia statute, it is clear that its regulation harmonizes with and is nicely adjusted to actual existing practices. If the statute requiring payment of commissions and countersignature by a commission agent had been made applicable to mutuals, it would have completely disrupted their customary methods of doing business, because they do not pay commissions and have no commission agents who could countersign. On the other hand, the stock companies do have commission agents and do not pay commissions to their salaried employees. The requirements, therefore, are perfectly adapted to their practices. Nor are the appellant companies objecting to the prohibition against their paying commissions to their salaried employees. The only substantial objection they are making is to the requirement that commission agents must countersign their contracts and be paid commissions on contracts negotiated in New York and elsewhere outside of Virginia.

This question is one which was in no way involved in the *Harrison case*. No mention was even made of the practices of stock companies with respect to nonresident brokers, nor of the necessity of regulating such practices.

If this practice is to be regulated by the State there is no other effective manner in which it can be accomplished than by the requirement that the resident commission agent countersign and receive substantial compensation for his services as an associate agent. If the countersignature provision should be eliminated, there would remain no method by which the State could enforce its requirement for the association with such contracts of an impartial commission agent. The appellant companies have admittedly violated persistently the provisions of the

Virginia Insurance Commissioner's regulation prohibiting hotchpotch contracts, and the only possible means of enforcing this regulation, as well as preventing rate discriminations and rebates, is through the countersignature requirement. Not only is this requirement adapted to the customs and practices of the appellant companies, but it is the *only* method by which the desired purposes of the regulation can be effectually accomplished. Certainly, if this is the only means available, it cannot be said to be arbitrary or unreasonable.

E. The Appellants are not Harmed Because the State does not Require Mutual Companies to Compensate Their Agents on a Commission Basis.

In *Clark* v. *Paul Gray, supra,* this Court said the appellees in that case could not "take advantage of an alleged discrimination which, if it exists, does appellees no harm." In the case at bar the appellants make no claim that they are harmed by the failure of the statute to compel the mutual companies to change their existing basic principles of doing business through salaried agents and substitute therefor commission agents. As heretofore pointed out the appellants probably would not desire a statute so providing.

There was some suggestion in the testimony of one or two of appellants' employees that the requirement that the Virginia resident agent be paid one-half the producers' commission might result in brokers placing business with mutual companies but this was not borne out by the testimony of the broker witnesses themselves. They stated that they would not place their clients in mutual companies because the service they provided was unsatisfactory. Certainly there is no proof in the record that the appellants will suffer any substantial harm from

mutuals by reason of this statute. The same practice prescribed by the statute has been followed by stock fire insurance companies for many years, and the stock fire companies enjoy a larger share of the total volume of fire insurance business than the stock casualty companies do of the total casualty business.

As above mentioned the *Harrison case* is not authority for the proposition that mutual and stock insurance companies may not be separately classified for regulatory purposes, where there is a conceivably rational basis for the particular regulation enacted. On the contrary, the Supreme Court has held exactly the reverse. In *German Alliance Insurance Co.* v. *Lewis*, 233 U. S. 389, the statute of Kansas fixing premium rates was attacked as unconstitutional upon the ground that it exempted from its operation farmers' mutual insurance companies insuring only farm property. The court said:

> "The provision of the statute is, 'That nothing in this act shall affect farmers' mutual insurance companies, organized and doing business under the laws of this State, and insuring only farm property.' The distinction is therefore between cooperative insurance companies insuring a special kind of property and all other insurance companies. It is only with that distinction that we are now concerned. There are special provisions in the statutes of Kansas for the organization of cooperative companies, and if the statute under review discriminates between them the German Alliance Company cannot avail itself of the discrimination. A citation of cases is not necessary, nor for the general principle that a discrimination is valid if not arbitrary, and arbitrary in the legislative sense, that is, outside of that wide discretion which a legislature may exercise. A legislative classification may rest on nar-

> row distinctions. Legislation is addressed to evils as they may appear, and even degrees of evil may determine its exercise. *Ozan Lumber Co.* v. *Union County Nat. Bank*, 202 U. S. 623. There are certainly differences between stock companies, such as complainant is, and the mutual companies described in the bill, and a recognition of the differences we cannot say is outside of the constitutional power of the legislature. *Orient Ins. Co.* v. *Daggs*, 172 U. S. 557."

See also in this connection *Supreme Council Royal Arcanum* v. *Behrend*, 247 U. S. 397, 399, and *United States* v. *Rock Royal Cooperative*, 307 U. S. 533.

F. The Bill of Complaint does not Raise the Question of Equal Protection

The appellant companies have not complained that they will suffer or be in any way damaged as a result of any discrimination against them in favor of mutual companies which would deprive them of the equal protection of the laws. It is well known that with one or two immaterial exceptions mutual companies do not pay commissions to their soliciting agents at all, but compensate them solely on a salary basis. The Virginia statutory provisions as to countersigning by a commission agent and paying him the commissions could not apply to mutual companies which have no commission agents unless their fundamental practice in this respect is to be completely changed by statute. Such a change would be a revolutionary one in the insurance business. On the other hand, the appellant companies do not pay commissions to their salaried branch managers, special agents or other employees. The undisputed customs and practices which control their respective methods of doing

business have clearly established this distinction between them. The appellant companies' premium rates contain a factor dedicated to the payment of commissions, the mutual rates do not. Stock companies do not negotiate contracts directly with an assured without paying to either a commission agent or a broker the producer's commission embraced in the premium (Op. R. 47).

Therefore, as to business *produced in Virginia,* the appellant companies only complaint of the statute is that they may occasionally be inconvenienced by their branch managers or other employees not being permitted to countersign contracts. As to this domestic business there is no complaint that this will add to the commissions appellant companies have been accustomed to pay Virginia resident commission agents. They admit they have invariably paid all commissions to such commission agents. These commission agents, for licensing purposes, are designated "Resident Agents," but the branch managers, Special Agents and Company Employees are all entitled to be licensed and to solicit business and perform every other function of a "Resident Agent" except countersign policies. The only act a mutual agent may do for his company which a branch manager or special agent of a stock company may not do for his company is countersign contracts.

While the existence of the above facts is shown beyond dispute in the record, the evidence showing them was not adduced in support of any issue relating to equal protection against mutuals. The complaint raises no such issue of fact. On the contrary, the complaint expressly states that the appellant *companies* do not even claim they have been denied equal protection of the law. They admit they have not. The last sentence of paragraph 9 of the Complaint is as follows:

> "The plaintiffs do not claim that any provision of the said 1938 Act violates the rights of the *company* plaintiffs *because of denying them the equal protection of the laws,* nor that any provision thereof violates the rights of the *agent* plaintiffs because of such denial except for the reason as shown in paragraph (11) hereinafter." (Complaint, p. 14. Italics supplied.)

This allegation is clearly one of fact, and, in substance, is that, *as a matter of fact,* the distinction in the statute between the countersigning authority of mutual agents and employees and stock company agents and employees does not hurt the appellants and does not deprive either the branch manager or company appellants of equal protection.

The only claim the *branch manager* appellants make in their complaint as to denial of equal protection is based upon an alleged discrimination between them and the *commission agents of stock companies* in that the branch managers are not permitted to provide the requisite countersignature while the resident agent may. The last sentence of paragraph 11 of the Complaint is as follows:

> "* * * The regulation and limitation having the effects as stated in sub-paragraph (a) of paragraph (8) is void whether undue, unreasonable, and arbitrary, or otherwise, because not bearing equally upon the agent plaintiffs and registered resident agents." (Complaint, p. 17).

This allegation applies to the *branch manager* appellants only, because the above quoted allegation from the last sentence of paragraph 9 completely eliminates the *company* appellants from the allegation with respect to

equal protection and renders it applicable *only* to the *branch managers*. The regulation referred to above in sub-paragraph (a) of paragraph (8) relates only to the countersigning provision. There was no question of discrimination between commission agents and salaried employees of *stock companies* decided in the *Harrison case*.

It is elementary that the appellees are not required to either answer or introduce evidence bearing upon a factual issue *not raised by the complaint*. *A fortiori* is this true where the complaint expressly *admits* that no company appellants are damaged or hurt by any lack of equal protection *as against mutuals, their agents and employees*. As above pointed out, the *Harrison case* is not decisive of the existence or non-existence of facts in Virginia which would show the reasonableness of Virginia's classification of stock and mutual agents, because the statutes are essentially different and the facts before the court are different. Certainly there are many relevant facts in this record which were not presented to or considered by any of the courts in the *Harrison case*. None of the evils incident to rebating by New York brokers, rate violations through hotchpotch contracts, preferential rates accorded New York brokers by stock companies in experience rating, nor the perfunctory manner in which the branch managers in Virginia have discharged their countersigning duties were suggested to the courts or considered by them in the *Harrison case*.

In fact, no countersignature provision was even mentioned. The question presented on the record in that case is not even similar to that arising from the facts here, and even if these company appellants had not admitted in their pleadings that they were not hurt or damaged by any want of equal protection because of discrimina-

tion in favor of mutuals, and even if they had expressly claimed same, the *Harrison case* would not be even a persuasive authority in support of such a position.

Furthermore, even if this Court should be of opinion that the appellant companies will be damaged by the failure to require mutuals to have their policies countersigned by resident commission agents, it would be clearly beyond the province of the court to inject into the case an entirely new question, one not only not embraced in, but expressly eliminated from the case by the allegations of the Bill of Complaint. As said in the case of *The Fair* v. *Kohler*, 228 U. S. at p. 25:

> "Of course, the party who brings a suit is master to decide what law he will rely upon, and therefore does determine whether he will bring a 'suit arising under' the patent or other law of the United States * * *."

The appellants here have decided in their complaint not to bring this suit under the Equal Protection clause of the Federal Constitution. The evidence has been taken by both appellants and appellees only with relation to the matters complained of to the court. To decide the case on any other ground of attack, involving factual questions, would be to decide an entirely different case from that presented by the complaint, answer and evidence.

CONCLUSION OF PART I.

It necessarily follows from the evidence in this case, and the legal principles established by the decisions of this Court hereinabove cited, that the making of a Virginia coverage insurance contract by a nonresident foreign corporation, licensed to do an insurance business in

Virginia, is an exercise of the privilege granted by his license, and that Virginia has jurisdiction to regulate the doing of all acts in Virginia pursuant to said contract; that Virginia may revoke or suspend any such license or impose a fine upon the licensee for exercising the granted privilege in such manner as to violate her laws, either in the making or in the performance of said contract; that the statutory regulation here under attack is intended to and will remedy, in whole or in part, and discourage the evil practices of rebating of rates by insurance company licensees and the rebating by New York brokers of their commissions to assureds with the active connivance and assistance of said licensees, as well as adjust the unequal and unfair competitive advantages enjoyed by nonresident brokers over Virginia resident insurance agents, by foreign group insurance companies under hotchpotch contracts over domestic insurance companies which have no group affiliations, and by large national corporations in their reduced insurance costs over locally owned independent businesses and industries, and that said statutes are not unduly discriminatory but are reasonable and well adapted to the purposes sought to be accomplished.

PART II.

Reply to Appellants' Brief

APPELLANTS' THEORY OF "QUESTIONS PRESENTED"

Appellants divide the questions presented, as they conceive them, into three statements (Appellants' brief, 3-4).

The statement of the first question is predicated upon a legal interpretation of the challenged statutes contrary to that placed on them by appellees, who are the officers of the State charged with their enforcement. Appel-

lants state that the statutes have the effect of "prohibiting the corporate appellants from making such a contract in a state other than Virginia." This interpretation appellees have shown to be erroneous, *supra,* pp. 25-6.

Appellants' statement of the second question recognizes that they may lawfully make insurance contracts outside of Virginia if countersigned by a resident Virginia agent, and he is paid the required commissions, and appears to be a correct statement of the question.

Appellants' statement of the third question presented may also be accepted.

APPELLANTS' STATEMENT OF "THE PURPOSE OF THE STATUTE"

Appellants contend that the sole motive of the statute was to "save for Virginia local agents commissions justly theirs," and to "get them what they wanted." This may have been the chief purpose dominating the agents in advocating the legislation, but this Court has consistently refused to consider motives attributed to a legislative body by parties litigant. The purposes of the statutes have been fully discussed, *supra,* p. 69, *et seq.*

APPELLANTS' STATEMENT OF "THE FACTS"

Appellants contend in their brief (p. 7) that the producer may place contracts with a mutual company not within the statute. But there is no incentive so to do, because mutuals, with immaterial exceptions, do not pay commissions (Op. R. 65). Appellants' witness Nichols, a New York branch manager, knew of only one large mutual paying same (R. 123), and, even in the exceptional cases where commissions are paid by mutuals, the appellants' broker witnesses testified that because of poor service rendered by them or for other reasons they will

not place contracts with them (R. 811-2, 877-8). It is a matter of common knowledge that the rate of commissions paid by the few mutual companies which pay any at all, is so much smaller than that paid by the stock companies that the brokers would not profit by placing their business with them.

At page 14 of the appellants' brief, it is said that a local resident agent is never associated with the writing of casualty and surety contracts. This is contradicted by two of appellants' witnesses, Izard (R. 632) and Yancey (R. 680-1), Virginia agents, who testified they were frequently associated with brokers in such contracts.

Appellants state in their brief (p. 15) that the New York brokers will not render the same service for half their present commissions and therefore the company will have to pay them the amount of the half received by the Virginia agent. But this leaves out of consideration the fact that the service the Virginia agent will render will make it unnecessary for the broker to give the same service as in the past. The compensation is divided and the work will be likewise divided.

Appellants complain (brief, p. 16) that the statute imposes no obligation on the Virginia agent to render any service in contracts produced outside the State. Neither does the statute expressly impose any such obligation with respect to contracts negotiated within the State. The same identical provision applies to them all, and the appellees have construed the statute as imposing on the agent the same duties with respect to contracts produced outside the State that custom has imposed on him in cases where he himself negotiates the contract. The Virginia agents have likewise construed the statute. (See discussion, *supra*, p. 89, *et seq.*)

Appellants' argument with respect to the facts is apparently predicated upon the theory that the burden rests on the State to prove that the resident agents will render services commensurate with the compensation they will receive. But the appellants challenge the constitutionality of the statute on the ground that it is arbitrary or capricious and the burden is on the challenger to rebut this presumption *by proving that no conceivable fact or state of facts exist* which can possibly constitute a permissible basis for the legislation. *Borden's Farm Products Co.* v. *Baldwin*, 293 U. S. 194, 209, 79 L. ed. 288. The appellants' argument on the factual question is restricted solely to the one thought, that the *only conceivable purpose* of requiring impartial resident agents to countersign the contract and be paid half the commissions is to unjustly enrich the agents at the appellants' expense. They do not even consider whether it might not be a legitimate purpose of the legislation to prevent rebates and rates discrimination; to adjust competitive inequalities and unfair competition between Virginia agents and nonresident brokers, or between the independently owned small Virginia merchant, industrialist or business man, and his competing national corporation, or between the Virginia fire insurance company or casualty or surety company, and foreign affiliated groups writing one hotchpotch contract combining all these coverages in disregard of premium rates fixed by Virginia law. Nor do they consider the existence of a *conceivable state of facts* under which the independent impartial agent might be utilized by the State as a watchdog or policeman over the insurance companies to prevent them from making, in or outside Virginia, hotchpotch contracts or from violating Virginia rate and rebate laws, or other legal requirements. In 1921, eighteen years ago, a regulation

was issued by the Virginia Commissioner of Insurance, which was intended to prohibit insurance company licensees from making these hotchpotch contracts. It contained this provision:

> "All forms of insurance against loss or damage on persons and property located within the boundaries of the State of Virginia shall be issued under a policy which shall be separate and distinct from all insurance which covers persons and property located in any other State. All insurance, whether excess, floater, blanket, general (reporting) cover, schedule, group or any form which has for its object the insurance of risks in the State of Virginia in connection with risks in other States, shall be held to be included under this rule" (R. 543).

The Insurance Commissioner evidently was aware of the evils attending these practices which still prevail in spite of his efforts to prevent them. A few days later he promulgated another interpretative ruling, in which was emphasized the necessity for countersignature by a Virginia resident agent and the payment to him of his usual commission. The ruling stated further, however, that it was permissible for a *salaried resident agent*, licensed by the bureau, to provide the required countersignature. This fact,—that the salaried agent could countersign,—doubtless accounts for the insurance companies having completely ignored the regulation. The resident commission agent would hardly have dared risk the revocation of his license by so flagrantly violating the ruling of the bureau as to countersign hotchpotch contracts, or parts thereof.

But, as stated, the appellants have completely ignored the conceivable existence of a state of facts which would

justify the enactment of the challenged legislation other than the one fact (and this is really not a fact but a speculation as to future action of agents) that the agents will not or may not render services to the insurer and the assured commensurate with the compensation he will receive, and that it is not desirable that they should render same. That this omission to prove the non-existence of such other facts, or states of facts, is fatal to their case, is conclusively established by the Supreme Court's decision in the case of *Pacific States Box and Basket Co.* v. *White*, 296 U. S. 176, 80 L. ed. 138. The Oregon Department of Agriculture had promulgated a regulation prescribing certain types of containers for the marketing of strawberries and raspberries. The plaintiff box company sought an injunction from the Federal District Court against the enforcement of the regulation on the ground that it was arbitrary and unreasonable and granted a monopoly to manufacturers of other types of containers. The case was heard on a motion for a preliminary injunction and the defendants' motion to dismiss the bill. This raised directly the question of the sufficiency of the allegations of the bill to negative the existence of any state of facts which would render the legislation proper. On this question the court said:

> "Plaintiff contends that since the case was heard on motion to dismiss the bill, all allegations therein made must be accepted as true; and, among others, the charge that 'there is no necessity for the particular orders relating to strawberries or raspberries' 'based on considerations of public health, or to prevent fraud or deception, or any other legitimate use of the police power, and the particular container described * * * does not of necessity promote, pro-

tect, further or develop the horticultural interests of the State;' and that its necessary effect is 'to grant a monopoly to manufacturers of the so-called hallocks.' The order here in question deals with a subject clearly within the scope of the police power. See *Turner* v. *Maryland*, 107 U. S. 38, 27 L. ed. 370, 2 S. Ct. 44. *When such legislative action 'is called in question, if any state of facts reasonably can be conceived that would sustain it, there is a presumption of the existence of that state of facts*, and one who assails the classification must carry the burden of showing by a resort to common knowledge or other matters which may be judicially noticed, or to other legitimate proof, that the action is arbitrary.' *Borden's Farm Products Co.* v. *Baldwin*, 293 U. S. 194, 209. * * * *The burden is not sustained by making allegations which are merely the general conclusions of law or fact.* See *Public Serv. Commission* v. *Great Northern Utilities Co.*, 289 U. S. 130, 136, 137 * * *. *Facts* relied upon to rebut the presumption of constitutionality *must be specifically set forth.* See *Aetna Ins. Co.* v. *Hyde*, 275 U. S. 440 * * *; *O'Gorman & Young* v. *Hartford F. Ins. Co.*, 282 U. S. 251 * * *; *Hegeman Farms Corp.* v. *Baldwin*, 293 U. S. 163. A motion to dismiss, like a demurrer, admits only facts well pleaded. Compare *St. Louis, K. & S. E. R. Co.* v. *United States*, 267 U. S. 346, 349" (296 U. S. 176. Italics supplied).

And in *Clark* v. *Paul Gray*, 306 U. S. 583, 594, this Court said:

"* * * Hence, in passing on the validity of the present classification, it is not the province of a court to hear and examine evidence for the purpose of deciding again a question which the legislature has already decided. Its function is only to deter-

mine whether it is possible to say that the legislative decision is without rational basis * * *."

It is clear, therefore, that the appellants must *allege* in their bill and *prove all facts* necessary to *exclude the existence* of other *conceivable* facts or states of facts which would furnish a permissible ground for the legislation attacked.

Turning then to the complaint, it is pertinent to ascertain *what facts are alleged* which exclude the existence of any other *conceivable facts* which would sustain the legislation. Concisely stated, the complaint alleges the status of the branch manager appellants as "salaried agents" of the appellant companies, that prior to the present statute they were permitted by law to countersign policies; that the challenged statute now prohibits them from so doing, but requires this to be done by resident *commission* agents; that it requires said commission agents to be paid their customary commissions and to retain half of same, permitting the other half to be paid only to such nonresident brokers as are licensed in Virginia. The complaint then goes on to allege the injuries which the appellant companies and branch managers will sustain as a result of being required to pay commissions to Virginia agents on business negotiated outside the state, and that said injuries are in violation of their constitutional rights. The specific manner in which the appellants will suffer these various injuries is set out in detail in paragraphs 8 and 10 of the complaint.

The complaint alleges violation of due process in the application of the statute to contracts entirely negotiated and made outside the state, and these allegations are sufficient to properly raise the question of the *jurisdiction*

of the state to regulate the making or the performance of such contracts.

In addition to the question of the State's *jurisdiction*, the bill alleges a violation of the equal rights and protection of the *branch managers* in that the statute allegedly *discriminates arbitrarily* in favor of the commission agents in conferring on them the exclusive privilege of countersigning policies and contracts. The only facts alleged to support this claim of arbitrary discrimination are contained in paragraph 11 of the complaint.

Also, in addition to the question of the State's jurisdiction, the *company* appellants allege in the complaint that the provisions of the statute detailed in paragraphs 8 and 10, and allegedly injuring them as therein set out are "undue, unreasonable, arbitrary and void." The same facts as are alleged to support the branch managers' claim of *discrimination* are likewise alleged to support this claim of the companies that the statute is *arbitrary*, and are contained in paragraph 11. Since this paragraph contains all the allegations of facts contained in the bill upon which to base the charge of arbitrariness or of discrimination between branch managers and commission agents, for the convenience of the Court it is quoted here in full:

> "Each said regulation of the actions of any of the plaintiffs and each said limitation imposed upon the conduct of any of them in the exercise of a right to work and labor, or a right to conduct a business, by means of the said 1938 Act mentioned above, and by means of one or more provisions thereof, having an effect as stated in paragraph (8) above, is undue, unreasonable, arbitrary and void. Each of said provisions is designed exclusively to promote the interests of the general body of the Virginia stock fire,

casualty, and surety agents who are not registered company representatives of companies, with the view to unjustly enrich them at the expense of those who are so registered (by lessening the value of their services) at the expense of the companies (by increasing their operating costs and causing them losses of business) at the expense of the insuring public (by increasing the cost of insurance) and at the expense of the Commonwealth of Virginia, (by causing loss of the taxes on premiums on contracts covering in Virginia but produced outside of Virginia which will be placed in non-admitted companies). The unreasonable prohibition against the agent plaintiffs countersigning contracts, although they are in every respect qualified and entitled so to do is intended only to compel the company plaintiffs to secure countersignatures of their contracts covering in Virginia though produced outside of Virginia, from the Virginia registered resident agents. The unreasonable regulations of the furnishing of such countersignatures on such contracts are intended only to secure to them the payment of grossly excessive amounts of compensation therefor. The regulation and limitation having the effects as stated in sub-paragraph (a) of paragraph (8) is void whether undue, unreasonable and arbitrary, or otherwise, because not bearing equally upon the agent plaintiffs and registered resident agents."

It is quite obvious that these are not allegations of *fact* at all, but only of improper legislative *motives*. But the motive of the General Assembly in adopting this act may not be inquired into by the court.

"The decisions of this court from the beginning lend no support whatever to the assumption that the judiciary may restrain the exercise of lawful power on the assumption that a wrongful purpose or mo-

tive has caused the power to be exerted. As we have previously said: from the beginning no case can be found announcing such a doctrine and, on the contrary, the doctrine of a number of cases is inconsistent with its existence."

McCray v. *United States*, 195 U. S. 27, 55, 56, 49 L. ed. 78.

See also *Arizona* v. *California*, 283 U. S. 423, 455, and cases cited therein.

But even if considered as intended to allege facts, the allegations are not of *basic facts*, but of *conclusions of fact*, without any allegations of the existence of underlying facts to justify the conclusions alleged.

Under the rule laid down in *Pacific States Box and Basket Co.* v. *White* (quoted from, *supra*), these are not such allegations of fact as would operate to exclude the existence of other facts or another state of facts which would sustain the legislation, and which are presumed to exist.

If, therefore, this case were being heard solely on a motion to dismiss the complaint, which is as on a demurrer, there would be no proper allegations of fact before the court to sustain the charges that the legislation is arbitrary. The court could consider as to this, only such facts as are within the range of *judicial notice*.

However, in order to obviate the possibility that the court might judicially know facts which, standing alone, might lead to the conclusions appellants alleged, the appellees filed their answer. In paragraph 17 they alleged the interpretation which, as enforcing officers of the state, they placed upon the statutory provisions relating to the classification of commission agents and employees of insurance companies, as well as the general functions

of such agents and employees within their respective classifications. The answer (paragraph 17-d) sets out at some length the services which a commission resident agent customarily renders in connection with a contract he negotiates while paragraph 16-b alleges that the appellees construe the statute as imposing on the countersigning agent who is associated by the statute with a contract entirely negotiated outside the state "the same obligations with respect to supervising the contents and form of the contract, and with respect to future services to be rendered during the life of the contract, both to the assured and to an insurance company in connection therewith, as customarily apply in cases where the 'Resident Agent' himself negotiates a similar contract."

The fact of this interpretation by the appellees was proven by the witness Moore (R. 525-6), while the facts alleged as to services customarily rendered by commission agents was proven by the testimony referred to in Part I of this brief. In fact there was no contradiction in the testimony that the agent customarily renders services in the manner and of the kind alleged in paragraph 17-d of the answer.

The appellants in their depositions taken in chief sought to prove that the New York broker and the appellant companies' engineering and claim departments in Virginia render all the service necessary in connection with all contracts the broker negotiates and that there is no reason for the Virginia agent to render any service. This was evidently upon the theory that the statute, as construed and sought to be enforced by appellees, imposed the duty on the commission resident agent to render these services in connection with such contracts, but that this was arbitrary because there was no reason to require same.

In rebuttal the appellees introduced testimony to prove that the Virginia Association of Insurance Agents had taken the view that the agent *should* render the service, and also evidence to prove that the agents of the state will render same; that such service is desirable; that the custom of associating resident commission agents in out of the state produced contracts on a basis of equal division of the commission has prevailed for many years in the fire insurance business, and that in such cases these agents have customarily rendered such services.

Upon these two questions of fact—the desirability of and the probable rendition of these services—the great bulk of the testimony was taken. The appellants now assume that if the court should be of opinion that there is no desirability of such services and no probability that they will be rendered, then *there is no other factual basis upon which the legislation can be sustained.* But this necessarily assumes also that *the court cannot conceive* of any *other facts or state of facts* which would furnish a legitimate purpose for the legislation. The court, however, does not have to exercise any imagination in this case to conceive such other facts. Appellants contend that Virginia has no jurisdiction to say what kind of Virginia coverage contract the appellant companies make outside of Virginia, and no jurisdiction to require that rates fixed by Virginia law shall be adhered to in such contracts, and they even admitted in their brief filed in the District Court that these companies have never complied with the state's statutes requiring countersignature by Virginia licensed resident agents, even during the time their employees were permitted to provide the necessary countersignature. Furthermore, it appears from the evidence, and is not disputed, that the appellant companies have engaged generally in making hotchpotch contracts

in violation of the above quoted regulation of the insurance department, have engaged in rebating premium rates, and have acted as the medium for the rebating to the assured by the nonresident broker of part of the producer's commission factor which is loaded into the premium rate. These flagrant and wilful violations of Virginia laws have resulted in the evils set forth and discussed on pages 73-80, *supra*. It is also pointed out there the effect the statute here challenged will have towards remedying these evils. See page 75, ***supra,*** as to the Virginia countersigning agent's assistance to the state in enforcing anti-rebate laws, etc., in such cases.

Although the burden was on the appellants, by allegations in their complaint and by proof, to rebut the presumption of the existence of this state of facts attending the making of contracts in New York, they have neither alleged nor proven anything to rebut same. On the contrary, the existence of the facts was actually testified to by appellants' own witnesses. The truth is, instead of denying the existence of these facts the appellants claimed in the District Court that they have the right to grant rebates and discriminatory rates when the contract is made outside the state. It follows, necessarily, even aside from the testimony, from the fact alone that plaintiffs *deny* Virginia's jurisdiction to control the rates when the contract is made outside the state, that the court is not only justified in "conceiving" but must infer that this practice of rate cutting and rebating now exists and long has existed in the making of such contracts. And this necessary inference is further supported by the decisions of the New York courts which establish not only the fact that the practice of rebating by agents to assureds of part of the premium on risks domiciled in other states *is practiced in New York*, but also establish that such prac-

tice *is not in violation of the laws of that state.* In the case of *American Smelting & Refining Co. v. Stettenheim,* 164 N. Y. 235, decided in 1917, it appears that an insurance agent had made contracts with the Refining Company and others, under the terms of which he was to receive salaries aggregating $20,000 per year, but agreed to apply thereon all commissions earned on insurance placed pursuant to his employment, and also agreed to pay to his employers all such commissions earned *in excess of his salary.* The agent negotiated risks for his employers, some of the risks having their situs in New York and some in other states. The commissions on the risks domiciled in New York did not amount to more than the agreed salary. The agent paid to his employer-assureds commissions to the extent of his salary, but declined to pay to them the excess which resulted from commissions earned on risks, the situs of which was in states other than New York, on the ground that to do so would be a violation of section 65 of the insurance law of New York. This section prohibits any insurance company or agent from rebating to the assured any part of the premium "on property or risk located within this state, or against liability, casualty, accident or hazard that may arise or occur therein." The court rendered judgment in favor of the assureds, holding that the New York statute forbidding rebates by agents had no application to contracts covering risks having their situs in other states. The section of the statute involved in this case still contains the same language which the court construed as rendering it not applicable to rebates of premiums on risks covering in other states. Thus, it is not unreasonable to assume that this practice continues. As has already been pointed out, the requirement that contracts, negotiated in New York and other states, shall

be countersigned by Virginia *commission* agents and not by *salaried employees* of the insurance companies will be not only helpful, but is necessary, in order to bring the practice of rebating on Virginia coverage contracts within the measurable control of the State.

It is hoped the foregoing will serve to clarify the true issues and questions before the court in this case. Appellees will now proceed to reply to such parts of the appellants' brief as seem to call for answer, and, in so doing, will list the same headings used in said appellants' brief.

APPELLANTS' POINT I.

Appellants' statement of this point is as follows:

> "The Virginia Statute Prohibiting the Corporate Appellants from Making, Outside of Virginia, Contracts of Insurance and Surety Covering Persons and Property in Virginia, Is Unconstitutional and Void."

As appellees have hereinbefore pointed out (pp. 25-6, *supra*), the Virginia law enforcing authorities do not construe the statute as prohibiting appellant companies from making Virginia coverage contracts outside the State, and no such prohibition will be enforced. Appellees have shown, however, in Part I hereof, that the decisions of this Court clearly sustain Virginia's jurisdiction to impose reasonable regulations with respect to such contracts of insurance made by appellants outside the State when such contracts are made in the exercise of appellants' Virginia license privileges. The appellants in their brief (p. 19) deny that Virginia possesses such regulatory jurisdiction. They do not claim, as they did in their brief in the District Court, that these transac-

tions are of "no concern to her," but only that her jurisdiction does not extend to such contracts where same are "made in and according to the laws" of the state where made (p. 20).

It is obvious that Virginia is tremendously interested not only in the protection from unfair competition of her domestic insurance companies, her small or independent business industries and mercantile establishments, as well as her resident agents, but also in seeing that there is no discrimination made in rates or rebates of insurance premiums to the detriment of her own citizens. It is of vital concern to Virginia to protect her own citizens from the obviously unfair competition and increased insurance costs which result from giving preferential rates and rebates to national corporations operating industries and mercantile establishments and other types of business activities in Virginia in competition with Virginia citizens. It is also of great interest to Virginia that her insurance agents shall not be unfairly discriminated against in contracts involving insurance protection for these nationally owned competitiors covering their activities and operations in Virginia, which activities are carried on pursuant to a license privilege granted to such nationally owned competitors by this State.

At the outset, however, it should be made clear that Virginia is not claiming the right to prohibit the licensee insurance company from making Virginia coverage contracts outside the State in violation of Virginia premium rates and laws, in the sense that an injunction order could be secured to restrain such making. The licensee company doubtless may make such contracts just as an unlicensed insurance company may make them, and Virginia may have no jurisdiction to enjoin it. But the question here involved is as to the *legal consequences in*

Virginia of the doing of such acts by its licensee. Such acts persistently done *in the State* are unquestionably such a violation of the license privilege or franchise granted to the insurance company as to justify the State in revoking its license. But the appellant companies contend that they may make such contracts *outside the State,* and this strips Virginia of all power and jurisdiction to revoke their licenses. They claim that not only is the State without jurisdiction to revoke the offender's license, *but is compelled to permit the offender to perform in Virginia the contract made outside in violation of her laws.* Virginia's power to revoke the license is the precise question involved, because the prayer of the complaint is, in effect, that the appellees be restrained from revoking the appellant companies' licenses because of making such contracts outside the State while performing them inside by rendering inspection, engineering and claim service in connection therewith.

In support of their argument that the State is without jurisdiction to regulate Virginia coverage contracts made outside her borders, the appellants cite and rely upon a number of cases, some of them relating to a state's jurisdiction to tax or regulate such contracts, and others in the field of conflict of laws involving the question of whether the contracts shall be interpreted according to the *lex fori* or *lex loci contractus.* An examination of the cases cited, however, discloses that none of them was made *in the exercise of a license privilege to conduct an insurance business* in the state other than that in which the contract was made, where such other state was undertaking to tax or regulate, or its courts were engaged in construing the contract. These two types of cases will be discussed separately.

Cases cited by Appellants Relating to a State's Jurisdiction to Tax or Regulate

St. Louis Cotton Compress Company v. *Arkansas*, 260 U. S. 346, involved the validity of a tax imposed by Arkansas against the Compress Company, a manufacturing corporation, of 5% of the premiums paid by it to a *foreign insurance company NOT licensed* to do business in Arkansas. The contract was made outside the state but covered property located in the state. The Compress Company was a foreign corporation which was licensed in Arkansas. The court held the tax an attempt to regulate the activities of the *Compress Company* beyond the territory of the state, and that the state was without jurisdiction so to do. The making of such a contract was not an exercise of the Compress Company's license privilege to do a *manufacturing* business in Arkansas, while the insurance company with which it was made *had no license privilege to exercise.* This distinction is clearly developed in the *Tobacos case* (*Compania* v. *Collector*, 275 U. S. 87, heretofore discussed pp. 52-5, *supra*), which involved the validity of two separate taxes imposed on the *assured*, a licensed foreign *manufacturing* company. Both contracts were made outside the state but insured property in the state. (The word "state" is used because the court held the Philippine Islands occupied the status of a state in the case.) One of the contracts was made with a London insurance company, *which was licensed to do business in the state.* Losses under this contract were payable in London. The other contract was made with a Paris insurance company, *which was NOT licensed to do an insurance business in the state* with losses payable in Paris. The court treated the tax on the London company contract as though imposed directly on the insur-

ance company instead of the insured. The tax on the *licensed* London insurance company's contract was *sustained* on the ground that the making and carrying out of the contract involved *"an exercise or use of the right of the London Company to do business in the Philippines under its license."* The tax on the *unlicensed* Paris insurance company's contract was held invalid as an attempt by the state to tax or regulate the *Tabacos Company's activities outside the state.* The necessary conclusion is that making an *insurance contract* outside the state by a *manufacturing company licensee is NOT an exercise of its license privilege,* and cannot be taxed or regulated, but the making outside of the state of an *insurance* contract by an *insurance company licensee,* covering property in the state, *is an exercise* of the privilege of doing an *insurance* business in the state, and may be taxed or regulated by the state. This case clearly and unmistakably upholds the jurisdiction of the state, both to tax and to regulate the acts outside the state of a foreign corporaion where such acts are done *in the exercise of the corporation's licensed privileges.*

The *Allgeyer case,* 165 U. S. 578, cited by appellants, involved Louisiana's jurisdiction to impose on an individual *assured* a fine for making outside the state an insurance contract with an insurance company *not licensed* to do business in the state. The facts are practically the same as those in the *Cotton Compress case* and in the Paris insurance company contract in the *Tabacos case.* The effect of the decision is that the assured did not exercise a Louisiana license privilege in making the contract, and hence the state could not tax same.

Fidelity and Deposit Company v. *Tafoya,* 270 U. S. 426, cited by the appellants was a suit brought to restrain

the New Mexico Commission from suspending the right of an insurance company to do business in that state on account of the violation of a statutory provision which made it "unlawful for any insurance company authorized to do business in New Mexico to pay, either directly or indirectly, any fee, brokerage or other emolument of any nature to any person, firm or corporation not a resident of the state of New Mexico, for the obtaining, placing, or writing of any policy or policies of insurance covering risks in New Mexico."

New Mexico undertook to defend the validity of the statute on the ground that its purpose was to prevent payment of nominal commissions to resident agents in New Mexico of small sums for the use of their names; and that it was intended to secure responsible men to represent the company "on the spot." The court said in reply to this contention: "But whether such an interpretation would save the act or not it is impossible to limit it in that way. It forbids the payment of any emolument of any nature to any person for the obtaining, placing or writing of any policy covering risks in New Mexico. The words go beyond *any legitimate interest* of the state, and although the decree is based only on payments to agents *it* [the decree] *does not declare that the payments thus made prevented the payment of appropriate commissions to the agents in the state* nor does the statute limit its prohibition in that way." (Italics supplied.)

The necessary inference from the foregoing language is that, if the provisions of the statute has been restricted to accomplishing the purposes which they were intended to accomplish, such purposes would be of "legitimate interest" to the state. And the opinion of the court calls attention to the fact that the section had been repealed

by a new act "which substitutes the *more moderate requirement* that the policy must be delivered, the premium collected, and the full commission retained by an agent in New Mexico, with authority to that agent to employ a licensed nonresident broker to collect the premium, etc., and to pay him within limits." (Italics supplied.)

It will be observed that the new statute above referred to, which was passed in 1925 and has not since been challenged by the insurance companies, was quite similar to the statute here attacked in the case at bar, although the New Mexico statute went considerably further than the Virginia statute, in that it required the policy to be *delivered* and the premium *collected* by an agent *in New Mexico*. The reaction of this court to the new 1925 statute appears to have been quite favorable.

This brings us, then, to the second group of cases which will now be considered.

Cases Cited by Appellants Relating to the Interpretation of Contracts Where There is a "Conflict of Laws"

The appellees do not believe that the principles applicable to the interpretation of contracts where there is a conflict in the laws, and perhaps in the interests and public policies of two or more states, each of which is connected in some way with the making of the contract, the performance thereof or with its enforcement, have a controlling relation to the jurisdiction of a state to revoke a license privilege of an insurance corporation for its conduct in persistently making such contracts in violation of the license privilege granted. It may be said, generally speaking, and subject to some exceptions, that one state may not impose on the courts of another state any legal obligation to apply its laws in the interpretation of contracts, and while the full faith and credit clause is applicable in some cases where the contract is enforced in

a state different from that in which it is made, usually the problem is solved by the application of rules of comity and relative interest rather than of jurisdiction.

The case of *Aetna Life Insurance Company* v. *Dunken*, 266 U. S. 389, cited by appellants, was an action instituted in Texas upon a life insurance policy made in Tennessee at a time when the assured was a resident of that state. The insurance company was qualified to do business in Tennessee. The assured afterwards moved to Texas where he died and the beneficiary recovered judgment in the courts of that state for certain attorney's fees and damages provided for by the Texas statute but not by the statutes of Tennessee. The court held that it was beyond the power of the State of Texas to impose on the insurance company a greater obligation than that undertaken by it when it made the contract in the State of Tennessee, where the insured then resided. This contract was clearly made by the insurance company in the exercise of its license privilege granted to it by the State of Tennessee and was a *Tennessee coverage contract*. There can be little doubt as to the correctness of the conclusions reached that its interpretation and the obligations imposed thereby were controlled by the laws of Tennessee, since the contract was neither made in Texas nor in the exercise of a privilege granted by that state.

The appellants also cited the case of *New York Life Insurance Company* v. *Head*, 234 U. S. 149, but the appellees do not think a discussion of this case will throw any light upon the questions now before this Court. The conclusion there reached was obviously correct.

Appellants also rely on *Hartford Accident & Indemnity Company* v. *Delta & Pine Land Company*, 292 U. S. 143. The action was brought in *Mississippi* on a surety

bond which was negotiated in Memphis, *Tennessee,* which was the principal office *of the assured* in that state. The action was barred under the contract, as construed under Tennessee laws, but was not barred under the statutes of Mississippi, where the action was brought. The contract was a blanket bond covering any employee of the assured "in any position *anywhere.*" The court apparently reached the conclusion that the contract was not a *Mississippi coverage contract,* and therefore Mississippi had such a slight interest in the transaction that she would not be justified in construing the contract under Mississippi laws, though the court implied that if the reverse had been true, her laws would apply. The reasoning of the court is quite illuminating, so appellees will quote the pertinent portions of the opinion, which are as follows:

> "* * * It is true the bond contemplated that the employee whose faithfulness was guaranteed might be *in any state.* He was in fact in Mississippi at the date of loss, as were both obligor and obligee. The contract being a Tennessee contract and lawful in that state, could Mississippi, without deprivation of due process, enlarge the appellant's obligations *by reason of the state's alleged interest in the transaction?* We think not. Conceding that ordinarily a state may prohibit performance within its borders even of a contract validly made elsewhere, if the performance would violate its laws (*Home Ins. Co.* v. *Dick, supra,* [281 U. S. 408]), it may not, on grounds of policy, ignore a right which has lawfully vested elsewhere, *if, as here, the interest of the forum has but slight connection with the substance of the contract obligations.* Here performance at most involved only the casual payment of money in Mississippi. In such a case the question ought to be

regarded as a domestic one to be settled by the law of the state where the contract was made. A legislative policy which attempts to draw to the state of the forum control over the obligations of contracts elsewhere validly consummated and to convert them for all purposes into contracts of the forum, *regardless of the relative importance of the interests of the forum as contrasted with those created at the place of the contract*, conflicts with the guaranties of the Fourteenth Amendment. [Citing cases]. Cases may occur in which enforcement of a contract as made outside a state may be so repugnant to its vital interests as to justify enforcement in a different manner. Compare *Bond* v. *Hume*, 243 U. S. 15, 22. But clearly this is not such a case." (292 U. S. 143, 149. Italics supplied.)

It is very clear from what has been quoted from the foregoing opinion that the relative interests of the particular states most affected by a contract of this kind will and should be controlling as to the laws governing the interpretation thereof. If there is any question of *jurisdiction* involved, the determination of the question is not controlled by technical boundary lines, or by *where* the *contract was made*, but by considerations of the respective degrees of interest each state has in the transaction. With reference to insurance contracts covering risks in Virginia, New York would have no interest in the matter of compliance with Virginia's premium rates fixed by law, or in preventing rebates (as shown by her statute which is confined to domestic coverages) or in matters of unfair competition affecting persons in Virginia which may result from the contracts, while all these matters are of vital concern to the State of Virginia. It seems highly probable, therefore, in the light of what was said in the above case, that the courts would construe such a con-

tract in conformity with Virginia statutes even though made in New York. But, be this as it may, it is clear from the opinion above quoted that Virginia would not be compelled to recognize or permit the servicing or performance in Virginia of any such contract made in violation of her laws which would be prejudicial to the interests of Virginia and her citizens. The challenged statute has been construed by the Virginia authorities as requiring the appellant companies to associate with each such contract a resident commission agent for the purpose of servicing same, both before and after the making thereof. Appellants claim this requirement "penalizes" the companies, but this contention is obviously without merit. One purpose of the statute is to regulate the manner in which these contracts shall be serviced. This servicing consists of the agent familiarizing himself with the risk and examining the contract as to *correctness of coverage and rates, before countersigning.* Thereafter, during the life of the policy, the statute contemplates that the contract shall be *serviced jointly* by the company's engineers, inspectors and claim agents on the one hand, *along with the company's resident commission agent* on the other. How can it possibly be contended that the company is servicing the contract in compliance with these regulations when it omits entirely *that part* of the servicing which the statute contemplates shall be rendered by the company's *resident commission agent.* As construed by the Virginia Corporation Commission and Bureau of Insurance this statute is a *servicing regulation,* intended to require servicing by the resident commission agent along with such other servicing as the insurance company may provide. This agent's servicing, however, is an essential

The statute does not require the engineer, inspector or claim agent to service the contract. This latter is an implied obligation of the contract, but the *only* Virginia agent or employee which the *statute requires* to be engaged in servicing the contract is the resident Virginia commission agent. How, then, can the insurance company possibly service the contract in conformity with the statute without providing the services of the resident agent as the statute requires?

An interesting case (cited by appellants) in that part of the field of Conflict of Laws which relates to the jurisdiction of a state, through its courts, to change the legal rights and obligations of the parties under contracts made in other states, where nothing was done or contemplated to be done in the state of the forum and such state had no legitimate interest in the transaction, is *Home Ins. Co.* v. *Dick* (1929), 281 U. S. 397. After pointing out that the insurer was not licensed in Texas, where the suit was brought, that the contract was not made there and that the property insured was not located there, the court held that the judgment of the Texas court extending the agreed time within which suit must be instituted, and subjecting property to the payment of the claim, deprived the defendant of due process of law, citing, among others, the *Tabacos case* which has just been discussed. In a footnote Mr. Justice Brandeis said:

> "The division of this court in the *Tabacos* and *Dodge cases* was not on the principle here stated, but on the *question of fact* whether there were in those cases things done within the state of which the state could properly lay hold as the basis of the regulations there imposed. Compare *Bothwell* v. *Buckbee, M. Co.*, 275 U. S. 274, * * *; *Palmetto F. Ins. Co.* v. *Conn*, 272 U. S. 295, * * *. *In the ab-*

> *sence of any such things*, as in this case, the court was agreed that a state is without power to impose either *public* or *private* obligations on contracts made outside of the state *and not to be performed there*. Compare *Mutual L. Ins. Co.* v. *Liebing*, 259 U. S. 209, * * *." (281 U. S. 397, 408-409, fn.)

The clear inference from the foregoing, and the decision that in the *Tabacos case* the state of coverage had jurisdiction to tax the contract with the licensed London Company, which contemplated acts of performance in the state of coverage if losses occurred, is that in such cases the state of coverage may impose both public and private obligations on such contracts made outside its borders. The opinion in this case also said: "Doubtless the state may *prohibit the enjoyment* by persons within its borders of rights acquired elsewhere which violate its laws or *public policy*." (Italics supplied.)

Appellants also cite *Boseman* v. *Connecticut General Life Insurance Company*, 301 U. S. 196, which involved the question whether the laws of Texas or Pennsylvania controlled the interpretation of a group life insurance contract made in the latter state by an employer which covered an employee in Texas. The insurance company was not licensed in Texas when the contract was made and, therefore, was not exercising a Texas license privilege in making the contract. This Court held the contract should be construed according to Pennsylvania laws. There can be no doubt about the correctness of this decision.

Appellants argue (Brief, 31) that the case of *Great Atlantic & Pacific Tea Co.* v. *Grosjean*, *supra*, does not sustain Louisiana's jurisdiction to regulate the operation of the company's stores in other states, and that such a regulation would be parallel to Virginia's regulation of

contracts covering Virginia risks when made outside the State. But this Court has held in the *Tabacos* and *St. Louis Compress cases, supra*, that a foreign corporation, conducting an ordinary business under a license of a state, does not exercise its license privilege when making contracts outside the state, but an insurance company does when the contract covers risks within the state permitting acts of servicing or performance therein.

There can be no doubt that rights acquired under foreign made insurance contracts involving rebates or rate reductions do violate both Virginia laws and her public policy, and she may prohibit the insurance company licensee from enjoying such rights in Virginia by revoking its license to do business therein.

APPELLANTS' POINT II.

"Section 4226(a) of the Code of Virginia Prohibiting Appellants from Making Any Contract of Insurance or Surety on Persons or Property in Virginia if Solicited or Negotiated out of Virginia by a Person not Licensed by Virginia, Denies to the Appellants Due Process of Law, and is Unconstitutional and Void."

Again appellants seek to strengthen their position by placing on the Virginia statute a construction different from that given it by appellees in enforcing the law. It has been pointed out repeatedly that the appellees' answer and the testimony of the enforcement officer Moore construe the statute as permitting the appellants to pay a New York broker any compensation they desire for negotiating contracts. The only prohibition in connection with payment of commissions is against the agent, who is not permitted to divide his commission with any one in or outside Virginia, except a Virginia licensed

agent or broker. To allow otherwise would legalize rebating and would demoralize the business.

The Virginia statute does not prohibit appellants from issuing through Virginia resident agents contracts negotiated by nonresidents not licensed in Virginia, provided the Virginia agent countersigns the contract and is paid the customary commissions. This he may do at the request of the insurance company, and there is nothing to prevent the company from paying the nonresident broker, whether licensed in Virginia or not, any compensation it desires.

Appellants again cite *Fidelity and Deposit Company* v. *Tafoya, supra,* but appellees do not consider it necessary to add anything to their discussion of this case under appellants' "Point I," *supra.*

APPELLANTS' POINT III.

Reasonableness of Equal Division of Commissions between Virginia Agent and Nonresident Broker

The appellants argue that many Virginia agents are not nearly so competent as nonresident agents and brokers, and therefore their services would be of no benefit, but the statute contemplates that the assured will have the *joint services* of the local agent *and* the nonresident broker, as has been the custom in fire insurance. Furthermore, the assured or broker will have no difficulty in having the local agent of his choice associated with the contract, as any insurance company can easily secure the services of any particular agent by appointing him if he does not represent the company already. The agents do not represent any company or companies exclusively. Then, again, the members of the General Assembly were presumably acquainted with the qualifications of Virginia agents and their opinions on this question should

prevail over the opinions of appellants' salaried employee and broker witnesses, on which appellants base their arguments.

Appellants also argue that the services of the Virginia agent are not worth as much as those of the nonresident agent or broker who negotiates the contract and makes perhaps thousands of dollars as a result of a few days effort. Appellants probably have in mind the value of the rebate given by the broker, or his skill in securing discriminatory reduced rates by auctioning off the risk. However, that is one of the chief evils which the officers charged with enforcing Virginia's insurance laws hope the statute will remedy. Of course, this Court cannot undertake to measure the relative value of the services of the resident agent as compared with the nonresident broker, but the standard of fifty per cent of the commissions to each, which has been established by custom in the fire insurance business and has proven fair and satisfactory, is the only available yardstick. At any rate its adoption by the legislature cannot be said to be arbitrary and capricious in the absence of clear proof that the same practice would not be fair to the appellants. There has been no proof of any greater service to be rendered by a local agent in fire insurance cases. On the contrary, the evidence shows *more* need for it in the casualty lines (R. 361). In fact a fair reading of the testimony of all the witnesses leads to the irresistible conclusion that the local Virginia agent will render more and better service, service of greater value to all parties concerned, than the nonresident broker can possibly render without actually coming to Virginia.

Furthermore, the impartial Virginia local commission agent who is required to sign the contract can, under appropriate regulations of the insurance department, be

required to render the State department much valuable service in policing the writing of contracts and policies at the prescribed rates and in compliance with law, and in providing information upon which to base assessments of taxation against the companies. The agents can easily secure and, if required, report to the department the total amount of Virginia coverage premiums collected by all the insurance companies (R. 366-7, 430-1). Virginia taxes are assessed on premiums. There is a general belief among responsible Virginia agents that the insurance companies fail to report all the premiums for taxation (R. 427).

Appellants apparently argue that even if the State may properly require countersignature by a Virginia resident agent and provide reasonable compensation for what service he may render, yet it is arbitrary for it *to fix the basis* of his participation and this should be left open to agreement between the agent and the broker, or the agent and the insurance company. But this would entirely frustrate the purposes of the statute as the appellees conceive them. So-called "countersignatures" would either be auctioned off or a "dummy" agent appointed to countersign for a nominal sum. There would be no supervision of rates or contents of policies and contracts, and the policing function of the competent resident commission agent would be destroyed. No service would be rendered either to the insurer, the assured, or to the State in accident prevention work or other matters affecting the public interest, and the act of countersigning these contracts would remain a perfunctory matter as it was before the passage of this law. It is essential, in order to accomplish these purposes, that a fair standard of division of commissions be prescribed by law, and, as before

stated, the only yardstick available to determine this is the practice which has become established voluntarily in the fire insurance business. The appellants have been unable to distinguish favorably to their contentions between the extent or value of the servicing practices of the local agents in these various types of risks. After all, the agent has an incentive to make the amount of service rendered by him satisfactory to the assured and the broker, for if he does not, they will secure another agent when the contract is renewed, as well as in other contracts produced in the future. The appellees do not feel that there is cause to fear that the assureds and brokers will fail to secure services commensurate with the compensation received by the local agent.

Furthermore, the fact that the legislatures of many other states have adopted the same basis of equal division of commissions for the fire, casualty and surety businesses, is practically conclusive that this standard is a fair and reasonable one. In fact some states seem to have gone so far as to require all the producer's commission to be retained by the local agent. (See division VIII, *supra.*)

The appellants rely upon *West Coast Hotel Company* v. *Parrish,* 300 U. S. 379, (minimum wage case) in support of their argument that the standard of equal division of commissions is violative of due process. But the statute in that case fixed a minimum wage *definitely and affirmatively* predicated in part on something essentially *different* from the value of the services. In the case at bar certainly *no different basis than just compensation is prescribed* by the statute. If so, the appellants have not pointed it out. The *presumption* is that the legislature considered the practice of compensating the local agent on an equal basis with the broker which obtained in the fire insurance business also a reasonable standard to

adopt for surety and casualty insurance, and that there was no great difference in the service practices of local commission agents in the casualty and surety fields. The appellants have failed to prove that there is any difference favorable to their contentions. Their only reliance is on statements of their own salaried employees, and of brokers who do not want the Virginia agent to receive any part of the commissions, to the effect that in their opinions the Virginia agent will not fairly earn his share of the commission. The Virginia agents testify to the contrary. And under this state of evidence the appellants ask this Court to overthrow the findings of the legislature as to reasonableness and accept the speculative opinions of their prejudiced witnesses. The presumption is that the compensation of the Virginia agent is based upon the value of services to be rendered.

As said in the *West Coast case* (300 U. S. 379, 396):

> " 'The minimum wage to be paid under the Washington statute is fixed after full consideration by representatives of employers, employees and the public. *It may be assumed* that the minimum wage is fixed in consideration of the services that are performed in the particular occupations under normal conditions' (p. 396)." (Italics supplied.)

Although this Court *assumed* that the compensation was fixed "in consideration of the services" to be performed, yet appellants now ask the Court to assume exactly the opposite, or at least to find the opposite because the hostile brokers and salaried employees of appellants testify they are of a different opinion from the legislature as to the value of the local agents' services, and this also in the face of the contradictory testimony of the four agents, the resolution of the Agents Associa-

tion and the construction placed on the act by the Insurance Bureau and the Corporation Commission.

The effect of the decision in the *West Coast case* is to establish the proposition that, where in the exercise of the police power a state prescribes a standard of compensation for an agent or employee, the *quantum meruit* test is not the only one to be applied to determine the validity of the legislative action, and that there may be, as there are in the case at bar, other legitimate legislative purposes to be accomplished. In such cases the Court will not undertake to evaluate the services but will look to all the ends which may be achieved and consider whether, viewed in its entirety, the objects are so unrelated to the legislation as to necessitate the Court's holding same arbitrary and capricious.

Appellants express the fear that the brokers would place their business with mutual companies. But the statistical information filed by Mr. Moore, of the Bureau of Insurance, at appellants' request, shows that the *stock casualty* companies' premium business in Virginia for the year 1937 was $9,511,138, and the *mutual casualty* companies' premium business was $3,362,140 (R. 929, 932); while the *stock fire* insurance companies' premium business was $10,617,644, and that of the *mutual fire* insurance companies was only $1,398,365 (R. 929, 934). Thus the *stock casualty* companies transacted seventy-three per cent of the total casualty premium volume of Virginia, while the *stock fire* companies' premium volume was eighty-eight per cent of the combined total of *fire* insurance business. It is clear, therefore, that the practice of associating a resident Virginia commission agent on a basis of equal division of the premium has not only not been injurious to the *stock fire* companies as compared to the *stock casualty* companies, but has resulted in their transacting a much larger percentage of the total *fire*

insurance business than the *stock casualty* companies have transacted of the total *casualty* business.

The statistics, therefore, bear out the soundness of the contentions advanced by the high officers of the stock insurance companies quoted in appellees' original brief that the *best way* for the stock companies to compete with the mutual companies *is to provide the assureds with the very valuable services of the local commission agent.*

APPELLANTS' POINT IV.

The contention that the appellant branch managers are unduly discriminated against has been discussed under appellees' points VI and VII, *supra*, pages 108-113, and it is not desired to add anything to what is said there.

CONCLUSION

On the whole case it is clear that the appellant insurance company licensees cannot defeat or impair Virginia's jurisdiction to revoke their license privilege for violation of her laws by resorting to the device of going outside the State to violate said license privileges, so long as the acts done outside the State are done in the exercise of said privileges, and that the means employed by the statutes here challenged to prevent such violations are reasonable and appropriately adapted to accomplish a legitimate end; therefore the decree dismissing the complaint should be affirmed.

Respectfully submitted,

ABRAM P. STAPLES,
Attorney General of Virginia and, as such, Attorney for the Appellees.

March, 1940.

APPENDIX

The following numbered Virginia Code sections are set out in full in the appendix to appellants' brief at the pages indicated below:

Section 4180, pp. 63-5;
Section 4221-a, pp. 58-60;
Section 4222, pp. 49-52;
Section 4223, pp. 65-6;
Section 4226-a, pp. 52-4;
Section 4235, pp. 55-58;
Section 4235-b, pp. 60-2;
Section 4235-c, p. 62.

pp. 2, 5, 7,

SUPREME COURT OF THE UNITED STATES.

No. 592.—October Term, 1939.

William H. Osborn, Channing F. MacNeil, Lewis C. Adair, et al., Appellants,
vs.
Thos. W. Ozlin, William Meade Fletcher, and Lester Hooker, etc., et al.

Appeal from the District Court for the Eastern District of Virginia.

[April 22, 1940.]

Mr. Justice Frankfurter delivered the opinion of the Court.

Appellants have challenged the validity of a Virginia statute regulating the insurance of Virginia risks and have brought this suit to enjoin state officers from enforcing it. Its relevant provisions, copied in the margin,[1] forbid contracts of insurance or surety by companies authorized to do business within that Commonwealth "except

[1] The relevant portions of the Virginia statute are as follows: Section 4222. . . . (a) Insurance companies, legally authorized to do business in this State, except life, title and ocean marine insurance companies, shall not make contracts of insurance or surety on persons or property herein, except through regularly constituted and registered resident agents or agencies of such companies; no contract of insurance or surety covering persons or property in this State, except contracts of life, title and ocean marine insurance and except temporary binders covering other forms of insurance shall be written, issued or delivered by any such authorized insurance company, or any of its representatives, unless such contract is duly countersigned in writing by a resident agent or agency of such company; provided, however, that the countersignature of an insurance agency shall not be considered valid unless such countersignature be attested to in writing by a regularly constituted and registered resident agent of such company.

No State agent, special agent, company representative, salaried officer, manager or other salaried representative of any legally authorized insurance company, except a mutual insurance company, shall countersign any contract of insurance or surety, or any renewal thereof, covering persons or property in this State, except contracts of life, title and ocean marine insurance; provided that this section shall not apply to railroad companies and other common carriers engaged in interstate commerce.

. . . . . .

Section 4226-a. . . . . No resident agent or agency may write, countersign, issue or deliver any contract of insurance or surety upon persons or property in this State unless there shall be collected at the time the contract is written, issued or delivered, or within a reasonable time therafter, the full premium on such contract, and the resident agent or agency shall be entitled to and shall receive the usual and customary commissions allowed on such contracts, provided that such resident agent or agency may write such contracts at the request only of such other resident agents or agencies, when such agent or agen-

through regularly constituted and registered agents or agencies of such companies." § 4222, c. 218, Acts of 1938. Such resident agents "shall be entitled to and shall receive the usual and customary commissions allowed on such contracts," and may not share more than half of this commission with a non-resident broker. § 4226-a. Disobedience of these provisions (from which life, title and marine companies are exempted) may entail a fine or revocation of the corporate license in Virginia, or both. A district court of three judges, convened under § 266 of the Judicial Code as amended, 28 U. S. C. §.380, dismissed appellants' bill on the basis of elaborate findings of fact and conclusions of law, set forth in an opinion by Circuit Judge Soper. 29 F. Supp. 71. From this decree the case comes here on appeal under § 238 of the Judicial Code, as amended, 28 U. S. C. § 345.

The bill was brought by foreign corporations authorized to do casualty and surety business in Virginia, and by some of their salaried employees. It is their claim that the statute deprives them of rights protected by the Fourteenth Amendment of the Constitution. The exact nature of these claims will appear more clearly in the setting of the illuminating findings below which may here be abbreviated.

The "production" of insurance—"production" being insurance jargon for obtaining business—is, in the main, carried on by two groups, agents and brokers. Though both are paid by commission, the different ways in which the two groups perform their functions have important practical consequences in the conduct of the insurance business, and hence in its regulation. The agent is tied to his company. But his ability to "produce" business depends upon the confidence of the community in him. He must therefore cultivate the good will and sense of dependence of his clients. He may finance the payment of premiums; he frequently assists in the [redacted] of claims; he acts as mediator between insurer and assured in the diverse situations which arise. The broker, on the other hand, is an independent middleman, not tied to a particular company. He meets more specially the needs of

cies are properly licensed to transact the class of business involved in such exchange, and licensed non-resident insurance brokers who may be authorized by law to broker such contracts, and on exchange of business between resident agents or agencies in Virginia and licensed non-resident insurance brokers in other states the resident agent or agency in Virginia may allow or pay to such licensed non-resident insurance brokers, a commission not exceeding fifty per centum of the resident agent's or agency's commission allowed on such business.

large customers, using their concentrated bargaining power to obtain the most favorable terms from competing companies. His activities, being largely confined to the big commercial centers, take place mostly outside Virginia.

A policy, whether "produced" by broker or agent, must be "serviced"—an insurance term for assistance rendered a customer in minimizing his risks. To this end the companies exert themselves directly, but the "producer" may render additional service. Only to a limited extent can risks be minimized at long range; local activity is essential. When the contract is "produced" by a non-resident broker the "servicing" function is normally performed by the company exclusively. When the "producer" is a resident agent, the case is ordinarily otherwise. For this, as well as for other reasons, it is obvious that non-resident brokers prefer to negotiate their contracts covering Virginia risks with companies authorized to do business in that Commonwealth.

These basic elements in the insurance business attain special significance in the case of enterprises operating not only in Virginia but in other states as well. For them the brokerage system offers the attractions of large-scale production. Through what is known as a master or "hotchpotch" policy, the assured may obtain a cheaper rate by pooling all his risks, whether in or out of Virginia. This wholesale insurance may furnish not only a reduced rate but a reduced commission to the customer. These are advantages which naturally draw the Virginia business of interstate enterprises away from local agents in Virginia to the great insurance centers.

In affecting the cost of these master policies, say the appellants, Virginia is intruding upon business transactions beyond its borders. Not only is a licensed company forbidden to write insurance except through a resident agent, but the agent cannot retain less than one-half of the customary commission allowed on such a contract for what may, so far as the requirements of the law are concerned, be no more than the perfunctory service of countersigning the policy.

But the question is not whether what Virgina has done will restrict appellants' freedom of action outside Virginia by subjecting the exercise of such freedom to financial burdens. The mere fact that state action may have repercussions beyond state lines is of no judicial significance so long as the action is not within that

domain which the Constitution forbids. *Alaska Packers Assn.* v. *Comm'n.*, 294 U. S. 532; *Atl. & Pac. Tea Co.* v. *Grosjean*, 301 U. S. 412. Compare *Equitable Life Society* v. *Pennsylvania*, 238 U. S. 143. It is equally immaterial that such state action may run counter to the economic wisdom either of Adam Smith or of J. Maynard Keynes, or may be ultimately mischievous even from the point of view of avowed state policy. Our inquiry must be much narrower. It is whether Virginia has taken hold of a matter within her power, or has reached beyond her borders to regulate a subject which was none of her concern because the Constitution has placed control elsewhere. Compare *Wallace* v. *Hines*, 253 U. S. 66, 69.

Virginia has not sought to prohibit the making of contracts beyond her borders. She merely claims that her interest in the risks which these contracts are designed to prevent warrants the kind of control she has here imposed. This legislation is not to be judged by abstracting an isolated contract written in New York from the organic whole of the insurance business, the effect of that business on Virginia, and Virginia's regulation of it.

A network of legislation controls the surety and casualty business in Virginia. Insolvent companies may not engage in it. Virginia Code, § 4180. Neither companies nor agents may give rebates. § 4222-c. Rates for workmen's compensation, automobile liability and surety contracts are determined by its Corporation Commission. §§ 1887(75), 4326-a-1, 4350-3. The difficulty of enforcing these regulations, so the District Court found, may be increased if policies covering Virginia risks are "produced" without participation by responsible local agents. Rebates evading local restriction may be granted under cover of business done outside the state. Contrariwise, if resident Virginia agents are made necessary conduits for insurance on Virginia risks now included in master policies, the state may have better means of acquiring accurate information for the effectuation of measures which it deems protective of its interests.[2]

It is claimed that the requirement that not less than one-half of the customary commission be retained by the resident agent is a bald exaction for what may be no more than the perfunctory serv-

[2] Where out-of-state "production" actually leads to rebating in defiance of § 4222-c, there would seem little doubt of a substantial basis for Virginia's contention that the requirement of participation by a resident agent will make

ice of countersigning policies. The short answer to this is that the state may rely on this exaction as a mode of assuring the active use of resident agents for procuring and "servicing" policies covering Virginia risks. These functions, when adequately performed, benefit not only the company, the producer, and the assured. By minimizing the risks of casualty and loss, they redound in a pervasive way to the benefit of the community.[3] At least Virginia may so have believed. And she may also have concluded that an agency system, such as this legislation was designed to promote, is better calculated to further these desirable ends than other modes of "production."[4] When these beliefs are emphasized by legislation embodying similar notions of policy in a dozen states,[5] it would savor of intolerance for us to suggest that a legislature could not constitutionally entertain the views which the legislation adopts. Compare *Prudential Ins. Co.* v. *Cheek*, 259 U. S. 530, 537.

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the illegal practices more susceptible of detection and control. Cf. LaTourette v. McMaster, 248 U. S. 465. Virginia has also contended that the master policy makes it possible for the companies to reduce their rates below the requirements of state law, and to attribute the reductions to risks in other states with requirements less stringent than those of Virginia. Appellants strenuously contend that no law of Virginia prohibits the reduction of rates for out-of-state risks to compensate for the higher rates which might be required by Virginia and, therefore, there is no illegal practice in this connection which the existence of a resident agent could aid in uncovering. This argument, if met on the merits, would lead us into the particularities of Virginia's rate laws. It is enough to say that even if these practices are not illegal, Virginia may have a legitimate interest in discovering the extent of their prevalence in order to devise, if she so chooses, effective laws to prevent them.

[3] See Hardy, Risk and Risk-Bearing, pp. 9-28, 66-67; Kulp, Casualty Insurance, pp. 188-91, 467-68; Michelbacher, Casualty Insurance Principles, pp. 448-78, 583-84; Crobaugh and Redding, Casualty Insurance, pp. 17-20; Huebner, Foreword to Modern Insurance Tendencies, 157 Annals of the American Academy of Political and Social Science, pp. 3-4; Burns, Service of Casualty Insurance, 15th Annual Meeting, Chamber of Commerce of the United States, p. 4.

[4] "The broker is not required to render any technical service beyond the placing of business." Michelbacher, Casualty Insurance Principles, p. 403. Compare *Id.*, pp. 401-402; Huebner, Property Insurance, pp. 81-96; Proceedings, 73rd Annual Meeting, National Board of Fire Underwriters, p. 123; Clark, Ellis and Fletcher, The Service of the Broker to the Assured in Liability Insurance, Howe Readings in Insurance, No. 18. But even if the broker does "service" the contract, his activities will take place in Virginia, and will affect the welfare of those inside Virginia who may be subject to the incidence of those risks which the "servicing" function tends to reduce. If this be true, it is Virginia's concern and not ours to prefer the agency to the brokerage method of "production."

[5] Alabama Code, § 8379 [as amended by § 980, Laws of 1939]; Kansas, General Statutes (Supp.), c. 40, § 246; Louisiana, Acts of 1918, No. 153; Maryland, Annotated Code, Art. 48A, § 65; Mississippi, Code, § 5205; Montana, Laws of 1937, c. 95; Oklahoma, Statutes Ann., Title 36, §§ 126, 142, 249;

The present case, therefore, is wholly unlike those instances in which a "so-called right is used as part of a scheme to accomplish a forbidden result." *Fidelity & Deposit Co.* v. *Tafoya*, 270 U. S. 426, 434. For it is clear that Virginia has a definable interest in the contracts she seeks to regulate and that what she has done is very different from the imposition of conditions upon appellants' privilege of engaging in local business which would bring within the orbit of state power matters unrelated to any local interests. It is not our province to measure the social advantage to Virginia of regulating the conduct of insurance companies within her borders insofar as it affects Virginia risks. Government has always had a special relation to insurance. The ways of safeguarding against the untoward manifestations of nature and other vicissitudes of life have long been withdrawn from the benefits and caprices of free competition.[6] The state may fix insurance rates, *German Alliance Ins. Co.* v. *Kansas*, 233 U. S. 389; it may regulate the compensation of agents, *O'Gorman & Young* v. *Hartf'd Ins. Co.*, 282 U. S. 251; it may curtail drastically the area of free contract, *Nat. Ins. Co.* v. *Wanberg*, 260 U. S. 71. States have controlled the expenses of insurance companies, New York Insurance Law, Consolidated Laws of New York, c. 28, §244, and Wisconsin Statutes, § 201.21; and see Report of Joint (Armstrong) Insurance Investigation Committee (N. Y.) pp. 403-18 (1906). They have also promoted insurance through savings banks; see Berman, The Massachusetts System of Savings Bank Life Insurance, Bulletin No. 615, U. S. Bureau of Labor Statistics, and New York Laws of 1938, c. 471. In the light of all these exertions of state power it does not seem possible to doubt that the state could, if it chose, go into the insurance business, just as it can operate warehouses, flour mills, and other business ventures, *Green* v. *Frazier*, 253 U. S. 233, or might take "the whole business of banking under its control," *Noble State Bank* v. *Haskell*, 219 U. S. 104, 113. If the state, as to local risks, could thus preempt the field of insurance for itself, it may stay its intervention short of such a drastic step by insisting that its own residents shall have a share in

South Carolina, Code, § 7972; South Dakota, Code, § 31.2218; Washington, Rev. Statutes, § 7080; Wisconsin, Statutes, § 201.44; Wyoming, Rev. Statutes, c. 57, § 203.

[6] See Gephart, Principles of Insurance, pp. 233-55; Dawson, Insurance Legislation (1895); Abstract of the Laws of Virginia in Relation to Insurance Companies, etc., issued by the Auditor of Public Accounts (1878); Patterson, The Insurance Commissioner in the United States.

devising and safeguarding protection against its local hazards. *La Tourette* v. *McMaster*, 248 U. S. 465. All these are questions of policy not for us to judge. For it can never be emphasized too much that one's own opinion as to the wisdom of a law must be wholly excluded when one is doing one's judicial duty. The limit of our inquiry is reached when we conclude that Virginia has exerted its powers as to matters within the bounds of her control.

In reaching this conclusion we have been duly mindful of the cases urged upon us by appellants. In *Allgeyer* v. *Louisiana*, 165 U. S. 578, apart from the doubts that have been cast upon the opinion in that case, the state attempted to penalize the making of contracts by its residents outside its borders with companies which had never subjected themselves to local control. Thus the statute was thought to be directed not at the regulation of insurance within the state, but at the making of contracts without. This was followed in *St. Louis Compress Co.* v. *Arkansas*, 260 U. S. 346; but see the refined distinctions drawn in *Compania de Tabacos* v. *Collector*, 275 U. S. 87. In *Fidelity & Deposit Co.* v. *Tafoya*, *supra*, the Court found that New Mexico had exceeded its power by forbidding "the payment of any emoluments of any nature to any [non-resident] for the obtaining, placing or writing of any policy covering risks in New Mexico". The Court was of opinion that this statute went "beyond any legitimate interest of the State. . . . ," *ibid.* at 435, but carefully withheld its judgment as to the validity of a later New Mexico statute not unlike the Virginia law here under review.[7]

The decree must be

Affirmed.

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[7] Hartford Ind. Co. v. Delta Co., 292 U. S. 143, resting on Home Ins. Co. v. Dick, 281 U. S. 397, held that the terms of a contract validly made in Tennessee could not be subsequently enlarged by Mississippi as to a condition of "substantial importance" when suit was later brought on the policy in Mississippi, simply because "the interest insured was in Mississippi when the obligation to indemnify . . . matured, and it was . . . . [the company's] duty to make payment there." 292 U. S. at 149. At the time the contract was entered into Mississippi had no interest in the risk covered. The Court felt that, even at the time of suit, "performance at most involved only the casual payment of money in Mississippi," *ibid.* at 150, and that was an interest so subordinate to that of Tennessee that the latter was entitled to have the right of way. No question was thus involved touching the right of a state to regulate companies doing business within its borders as to contracts of insurance covering local risks.

SUPREME COURT OF THE UNITED STATES.

No. 592.—October Term, 1939.

William H. Osborn, Channing F. MacNeil, Lewis C. Adair, et al., Appellants,
vs.
Thomas W. Ozlin, William Meade Fletcher and Lester Hooker, etc., et al.

Appeal from the District Court of the United States for the Eastern District of Virginia.

[April 22, 1940.]

Mr. Justice Roberts.

I am unable to agree with the decision in this case. I think it sanctions an exertion of power by Virginia over transactions beyond her jurisdiction.

Virginia may, of course, regulate the making of contracts of insurance within her borders. She may require such contracts to embody specified provisions. She may regulate the enforcement of these contracts in her courts. She may supervise and condition the activities of registered foreign insurance companies, agents or brokers within the Commonwealth. The statute in question has no such purpose.

The purpose and effect of the statute is to compel an insurance company which is a citizen of another state, and which negotiates a contract of insurance with an agent or broker within such other state, to pay a resident of Virginia for a service not rendered by him, but rendered by another in another state. By force of the statute a Virginia agent must countersign a contract negotiated outside of Virginia with an assured whose residence is outside of Virginia, which contract of insurance was negotiated by an agent or broker living outside of Virginia. The countersigning Virginia agent must be paid one-half the usual commission, even though the broker or agent who produced the business is licensed as a non-resident broker by Virginia, although the only service such Virginia agent is required to render and, in many cases all he does render, is the mere countersignature of the policy. With respect to this situation the court below said:

"We do not overlook the peculiar situation of the non-resident assured who form no part of the Virginia public which the state

desires to protect. Undoubtedly their business methods will be disturbed by the enforcement of the statute. It is contended, not without merit, that they have no need for the services of the resident commission agents, and that in fact, the latter cannot assume the function of producing agents in their behalf without harmfully intruding themselves into confidential business affairs. Moreover, it is fair to say that these affairs are so important and so widespread in their scope as to be beyond the technical knowledge and skill of the average Virginia agent, and that the interests of the non-resident assureds can be best looked after by the brokers at the great centers of population where the head offices of the insurance companies and of the assureds are located, and in Virginia by the engineering and claim personnel of the companies. It is also true that the substantial compensation required by the statute to be paid to the Virginia agents will increase the cost of the business."

The plain effort of Virginia is to compel a nonresident to pay a resident of Virginia for services which the latter does not in fact render and is not required to render. The principles underlying former decisions of this court are at war with the existence of any such asserted power.[1]

The CHIEF Justice and Mr. Justice MCREYNOLDS join in this opinion.

[1] Allgeyer *v.* Louisiana, 165 U. S. 578; New York Life Ins. Co. *v.* Head, 234 U. S. 149; Aetna Life Ins. Co. *v.* Dunken, 266 U. S. 389; Fidelity & Deposit Co. *v.* Tafoya, 270 U. S. 426; Home Ins. Co. *v.* Dick, 281 U. S. 397; Hartford Accident & Indemnity Co. *v.* Delta & Pine Land Co., 292 U. S. 143; Boseman *v.* Connecticut General Life Ins. Co., 301 U. S. 196.